HOWARD E. HAMMONDS, JR.

CURRENT ADDRESS:
P. O. Box 1797
Butler, PA 16003
TELEPHONE: (412) 282-4248

5'10" 175 pounds
DATE OF BIRTH: 12/30/43

SUMMARY OF QUALIFICATIONS:

Diversified Management and Administrative experience pertaining to management and marketing of sports and recreation products and services.

Seven years experience involving business relationships in more than thirty foreign countries, importing and exporting goods to and from these countries, consulting in the design of overseas recreational facilities, managing foreign personnel, instructing business development programs for large, multi-national firms, construction contract management and personnel training.

CURRENT POSITION:

Division Manager
D & H Marketing Services, Inc.
P. O. Box 349
792 Mercer Road
Butler, PA 16003
(412) 282-4248

PREVIOUS EXPERIENCE:

Director of Logistics and Construction
Riyadh International Community School
P. O. Box 990
Riyadh, Saudi Arabia
1979-1981

President - Chairman of the Board of Directors
International Marketing and Procurement Services, Inc.
P. O. Box 1797
Butler, PA 16003
(412) 282-2583

Responsible for all planning, construction, supervision and importation of physical facilities, equipment and supplies for school's, community of 2,200 students and staff.

Business Development Manager - Middle East
Niedermeyer-Martin Company
Portland, Oregon
1979

Company manager assigned to Middle East to develop market for company's products and services. Served as operations manager, developed new markets, provided bid quotation and do consulting work on recreation projects to architects, engineers and various government agencies.

Recreation Director
Morrison Knudsen Saudi Arabian Consortium
Al Balir, Saudi Arabia
1978-1979

Responsibilities included coordination and planning of all operational and administrative activities for the company's recreation program for a residential community of 10,000 workers and families. Liaison with logistic purchasing and marketing of various sport and recreation facilities. Planning and development of new facilities and programs.

Senior Athletic Director
Whittacker Corp.
Riyadh, Saudi Arabia
1976-1978

Responsible for development and implementation of training program of Saudi Arabia National Athletics team. Planning and administration support of the international competition program with various European, Middle and Far Eastern countries. Assist all logistic for personnel travel and training in various international competitions.

Instructor of Physical Education and Athletics
State University of New York - Plattsburgh
Plattsburgh, New York
1973-1976

Senior staff member responsible for planning, organization and implementation of University's athletics program. Also taught in the schools instructional health and physical education program.

Director of Athletics and Physical Education
Pennsylvania State University - Berks Campus
Reading, Pennsylvania
1968-1973

Responsibilities included program development, teaching physical education, planning and supervision of schools athletics and intramural programs.

Welder
Pullman Standard, Inc.
Butler, PA
1963-1968

INTERNATIONAL MARKETING AND PROCUREMENT SERVICES, INC.

COMPANIES REPRESENTATED BY

NAME AND ADDRESS	TELEPHONE TELEX ......CONTACTS....
ALUMINUM ATHLETIC EQ. CO. 4 PORTLAND ROAD WEST CONSHOCHECKEN, PA. 19428	TIM DRISCOLL 800-523-5471 215-825-6565
AMERICAN SHUFFLEBOARD CO. 210 PATERSON PLANK ROAD UNION CITY, NEW JERSEY 07087	RICH DELFINO 201-865-6633
DOUGLAS INDUSTRIES, INC. P.O. BOX 407 ELDRIDGE, IOWA 52748	1-800-553-8907 JERRY DOUGLAS 1-319-285-4162
GLOBAL GYM AND FITNESS 5711 STEELES AVE. WEST WESTON, ONTARIO CANADA M9L 1S7	416-749-7000 065-27342 TELEX JAMES (TED) BAKER VICE-PRESIDENT
JAYPRO CORP. P.O. BOX 400 WATERFORD, CT. 06385	ERNIE GOULET 203-447-3001 TWX 710-466-5912
LANDSCAPE STRUCTURES 601 7TH STREET SOUTH DELANO, MINNESOTA 55328	612-479-2546 910-5780833 TELEX STEVE KING, PRES. BARB KING, ACCTS. BRUCE LEMKE DENNIS NIELSON, ENG.
MEXICO FORGE P.O. BOX 565 REEDSVILLE, PA 17084	1-717-667-2157 STEVE RICHARDS, SALES LYNN CLINGER, DESIGN ENG.
CUSTOM STURCTURES, INC. P. O. BOX 1888 BUTLER, PA 16003	412-282-2712 CARL SLEAR

NAME AND ADDRESS	TELEPHONE TELEX ......CONTACTS....
PORTER EQUIPMENT CO. 9555 IRVING PARK ROAD SCHILLER PARK, ILLINOIS 60176	TOM CLARK 312-671-0110 259102270042 TWX
PENCO PRODUCTS INC. OAKS, PA 19456	JOHN WISSE 412-364-2100 CORP. OFFICE 215-666-0500 BILL MCFARLAND, ANDY BECK, SHIPPING
VIRCO MFG. CORP. P.O. BOX 5000 CONWAY, ARKANSAS 72032	1-501-329-2901 JOE LEHMANN

Mr. **Barnard**. Thank you very much, sir. We will now hear from Mr. Myron Miller, of Global Trade Services, Alexandria, VA. Mr. Miller.

STATEMENT OF MYRON MILLER, GLOBAL TRADE SERVICES, ALEXANDRIA, VA

Mr. **Miller**. Thank you, Mr. Chairman.

I'm honored to be asked here today to present my views, and I'll try to make them concise, from a somewhat different perspective than those of the other participants here today.

I founded Global Trade Services in 1985 as a consulting firm to assist companies which need to become globally competitive to meet both domestic and foreign competition, to assist companies which want to expand their foreign market presence and capabilities, and to help investors, multinational corporations, and banks establish new trading companies or improve their present trading companies.

My personal background has been one of 20 years involvement in the international field with the Singer Co., the Sunbeam Corp., Sears World Trade, and now with my own firm. I was the vice president of marketing and planning for Sunbeam's International Group which was responsible for all operations outside the United States; vice president of marketing for Sears World Trade when it was first formed in 1982; and was also managing director for Sunbeam in the United Kingdom and for the Singer Co. in Puerto Rico.

I have lived in the United Kingdom, Venezuela, and Puerto Rico, and have worked in 60 countries. My perspective is that of a person who has spent a fair amount of time traveling around the world to ensure that customers were identified and satisfied and to ensure that we met world class competitors. I have also had profit responsibility overseas, so I have that vantage point in international trade.

My views on the ETC Act, I think, have already been expressed by others. The GAO statistics now provide data on performance of ETC's not available when I was putting together my comments.

The low level of exports of ETC's, as you can see, is really a "drop in the bucket" compared to the problem of last year's $148 billion trade deficit and, as we learned the other day, a trade deficit of $16.5 billion just in January 1986. If you annualize the January deficit, you can see where we are headed in 1986.

A question was raised about the low level of output of the ETC's so far. Is it too early to judge whether or not the ETC legislation has been successful? One way to make that determination is to try to find one export trading company that you can use as a model of success. I can't find it.

In terms of some of the problems and barriers to success of export trading companies, one of the greater problems is the significant cultural difference between bankers and traders. They are very, very different kinds of people, and I think it is very difficult to reconcile the differences.

The same cultural difference problem applies to trading companies that are part of multinational corporations, because of the nature of a trader. In many cases there is little understanding, when people set up an export trading company or any kind of a trading company, of what a trader is. I have defined "trader" in my official statement.

I think that a very significant weakness of many export trading companies—and of trading companies in general—is that they have little understanding of the "critical mass" that is required to provide a service adequately for a customer.

If you examine trading companies, they are all different. If you look at the fullest range of the services of the Japanese Sogo Shosha, you will find a company that provides 25 different kinds of trade services, everything from countertrade, trade finance, project finance, acting as a distributor, even acting as a manufacturer, and in fact provides a "menu" of 25 different kinds of trade services. Any trading company you look at is some composite from a portfolio of trade services.

To perform any of those functions, whether it be countertrade, project finance, or trade finance, certain capabilities are required, but in many cases I've seen ETC's put a few people into a bank trading company and expect them to do what we had over 10,000 people to do overseas with Sunbeam and between 15,000 and 20,000 for the Singer Co.

To put into a company one person responsible for the entire Far East, and have that same person responsible for health care products worldwide, is only a "drop in the bucket" relative to the "critical mass" of capabilities that it takes to do business around the world. If you look at the staffing of the export trading companies that have been formed in recent years, you will see that after having acquired some fairly good internationally qualified people, they had a year or two of poor performance then spun off the operation or cut it back significantly.

An associate of mine was one of the latest people to be cut back in one of the significant bank trading companies on the west coast. That bank trading company cut back from the four or five significantly experienced international people they had hired a couple of years ago; they are back to having no nonbank people, and that trading company is only providing trade finance. I think that west coast experience is representative of the experience of bank trading companies along the east coast and in New England.

In many cases, there were unrealistic expectations about what was expected in terms of the numbers of companies which would be created because of the legislation. I agree with Ralph Chew that, in a way, the country went to sleep when the ETC legislation was passed back in 1982, and we somehow hoped that after a couple of years we'd wake up and everything would be fine in terms of the trade deficit and exports, and certainly that has not happened. I agree with Ralph's comments on the narrow scope of what was dealt with within the 1982 legislation and the broader scope of what is needed in future, legislation.

Another significant problem with regard to the ETC legislation is that many small- to medium-sized companies haven't been touched by the legislation. There has been a successful domestic company trying to get into international business. It takes hundreds of thousands of dollars to cross the "barrier" from domestic business to export business. The Japanese trading companies, for all their problems, have the worldwide infrastructure to help their domestic companies get into exporting.

Let me indicate some of the lessons we can learn from the Japanese.

If a small Japanese company wants to get into the international field, it can deal with any one of many trading companies with offices overseas. Just looking at the nine top trading companies in Japan, those companies have 900 offices outside of Japan. If the Japanese company wants to get into Frankfurt, it can deal with any of the nine companies which has an office in Frankfurt. They just have to pick the trading company that has the right "product fit" for them.

It's not just information that a small Japanese company gets from those offices. Those offices are able to transact business. While we may have certain Department of Commerce capabilities overseas to gather information, if some U.S. company wants to transact business, there is no vehicle for them to do that, whereas the Japanese offices can transact business.

Again, lessons from the Japanese—they are always competitive in their financing. Whether it is 6 percent or whatever, the Japanese are always competitive.

While we can't emulate the group relationship that the Japanese trading companies have with manufacturers and banks, we can at least learn from it. When you look at the profitability of the major trading companies in Japan, you always see a thin slice of profitability. You don't even need to ask what the profitability is this year. It's something less than 2 percent. The rest of their profits or losses are found either in the banks or in the manufacturers.

Nevertheless, because they take a group profitability approach, collectively they do a tremendous job in international trade, to our detriment.

The Japanese have patience. They don't just look for results in a couple of years. The reason that some of the ETC's have cut back is that bank managements have found that they don't want to live with the losses that they are sustaining and are now saying, "It didn't really fit our mission anyway; we've sold this unit off to some of the managers."

The Japanese trading companies do a tremendous job in grooming international people. They have people traveling around the world from assignment to assignment, picking up experience, which is tremendous in terms of their knowledge of markets and competition.

I saw an article the other day in U.S. News and World Report that indicated that Mitsubishi has 700 people in their New York office just dealing with gathering information on the U.S. market—700 people in just that one office, and they have other offices in the United States.

There are a total of 800 Americans working in Japan. That gives you a perspective on how you understand and work with markets.

With regard to the elements of success, there are some things to be learned from the Japanese in terms of having critical mass for the kinds of trade services that companies feel they need; having committed patient leadership from the management of the parent organization or the bank; having management that is willing not only to make a commitment in the first place but also to stay close to the operation until it is successful. The investors in the trading company should make sure, of course, that they have a good reason for establishing an ETC in the first place.

My final thoughts enhance what Ralph Chew said earlier.

I feel that better implementation or amendments to the legislation, if it's only done incrementally, is probably going to deal only with 5 percent of the problems and need to increase exports. I think we have a national crisis on our hands. With a $148 billion deficit in 1985 and heading toward $200 billion in 1986, and maybe $250 or $300 billion the following year, we have a national crisis, and I don't think that a softer dollar is going to reverse that.

You read articles in the paper saying, "Now that the dollar has dropped there's going to be a quick change." The trade flows may be reversed in commodities when the dollar softens, but all the companies in the last couple of years that have gone into out-sourcing or have established manufacturing facilities overseas aren't going to change very quickly, and the labor rate disparity is still so great in many cases that they wouldn't bring manufacturing back to the United States.

All the manufacturing of computer peripheral equipment is being done outside the United States. Harris was one of the last companies to give up the ghost on manufacturing computer peripherals in the United States. That process is not going to reverse quickly. The factories are closed, and the people who were doing that work are gone.

What I'm finding is that there are many companies just beginning to understand the benefits are of out-sourcing and learning how to do it. We may see an increase in out-sourcing rather than a decrease, because of the increased knowledge and courage people have to out-source.

I think we need a Manhattan project to deal with the trade deficit. Granted, it has to be the private sector that increase exports, but there has to be encouragement from the appropriate kinds of trade legislation, whether it's Senate bill 1934 or the Trade Enhancement Act, S. 1860. There has to be a clear indication that dealing with the trade deficit and increasing exports is a high national priority and that we are really going to do something about this issue.

I suggest that information be assembled—through a task force—about what is being done throughout this country to enhance exports. There is good work being done by many cities, States, trade associations, et cetera. I've had a chance to speak before groups like the Southern California Foreign Trade Association, the Upper Penninsula Forest Products Association and many others. There is great interest in increasing exports. There are a lot of groups trying to increase exports, but we're not getting our fragmented effort together in a way that will deal efficiently with the crisis.

Among the issues that I think a task force should address—given a recognition of the trade deficit as a national crisis and that the United States is in a trade war that we are in the process of losing—are that we have to match some of the Japanese trading strengths, realizing we have a different culture, and a different business environment. Nevertheless, we have to match many of their capabilities if we are going to be as effective in trading as they are.

We have to find a way of providing smaller companies with what I would call pretrade advisory services, to assist small companies that would like to get into international operations but face the barrier of the several hundred thousand dollars required to get into exporting. Some significant effort must be directed toward assisting small businesses in their efforts to export.

When you talk about the difficulty of how ETC's can benefit from the ETC Act and what smaller businesses must do to benefit from the legislation, it's not that easy to find information. I think the small businessman has to be the subject of some real missionary efforts on an ongoing basis to help them overcome the barriers to exporting.

The incentives for exporters or for ETC's are very important. Ralph mentioned this in his comments in the booklet on the trade deficit, and I understand it's going to be included in this record, too. There is some real content and some issues in that booklet that need to be dealt with.

We could even look at the other side of the trade deficit problem. What kind of incentives could be provided for import substitution? Could there be something you could do for the shoe industry or for textiles that would incentivate them to invest in manufacturing processes that would make them be able to be competitive in this country?

Some companies, for example, John Deere, put $1.7 billion into revitalizing their facilities. That's a lot of money. How do you incentivate others who may not have quite the capacity that Deere does to make that kind of investment?

In short, Mr. Chairman and members of the panel, I think we are facing a national crisis. I think that while there is merit to some improvements or enhancements that can be made to the ETC legislation, I, too—like Ralph Chew—would like to see legislative effort broadened far beyond the scope of the ETC legislation and beyond the amendments now being considered to deal with the crisis we face.

Thank you.

[The prepared statement of Mr. Miller follows:]

COMMERCE, CONSUMER, AND MONETARY AFFAIRS
SUBCOMMITTEE
OF THE
COMMITTEE ON GOVERNMENT OPERATIONS
CONGRESS OF THE UNITED STATES
HOUSE OF REPRESENTATIVES

MARCH 4, 1986

MYRON M. MILLER
GLOBAL TRADE SERVICES, LTD.

"THE IMPLEMENTATION AND EFFECTIVENESS
OF THE
EXPORT TRADING COMPANY ACT OF 1982"

I am honored to be asked to present my views to this committee on the implementation and effectiveness of the Export Trading Company Act of 1982. This testimony comes at a particularly critical time, since we have just learned that the U.S. trade deficit for January 1986 was $16.5 billion, thus accentuating the urgency of taking some decisive action to deal with the trade deficit, yet do it without increasing protectionism.

My vantage point on the effectiveness of the ETC Act of 1982 will be quite different from the others here to testify today, because of my particular background and because I want to avoid what I believe they are likely to present. I will begin by providing some information on my company and on my international trade experience.

Global Trade Services - Types of Service Provided

I developed my new business in 1985 based on the conviction that there are three major trade issues of the 1980's which present needs which my associates and I are equipped to meet:

1. We have entered a "new era of globalization," where every company, no matter what its size or location, is being drawn into world commerce and must be able to compete on a global basis. Therefore, companies must develop worldwide perspectives of their business and be able to compete effectively against the best companies in their industry throughout the world.

2. Despite some of the problems that trading companies are

facing throughout the world, there is still a very significant need for companies which can serve as trade intermediaries and creators of trade.

3. World trade is likely to increase dramatically through the rest of this century, so there is a need for a service which can develop new businesses with a global perspective and an orientation toward global competitiveness from the day they are founded.

The following services have been developed to meet these needs:

1. Services dealing with the need to be globally competitive:

   - For companies which need to defend themselves against world-class domestic and foreign competitors, reduce costs and increase productivity by:
     - Increasing productivity in domestic operations
     - Establish overseas sourcing capabilities for components or complete products
     - Establish new manufacturing facilities in the U.S. or overseas
     - Contract manufacturing
     - Import through trading companies which specialize in certian products
     - Establish joint ventures or acquisitions
   - For companies on the offensive in their market development, that is, those which want to enter foreign markets for the first time, for those now marketing overseas but want to expand into new markets, and for companies wanting to be more global in their operations, assist them in:
     - Exporting through agents, distributors, or export trading companies
     - Establishing sales and marketing subsidiaries
     - Establishing job-creating manufacturing subsidiaries when that is required for market entry
     - Development and introduction of new products worldwide
     - Licensing
     - Improving market share in existing markets
     - Licensing

- Joint ventures or acquisitions

2. Services for those who want to establish some type of a trading company, or for those who want to use a trading company:

   - Assist in the determination of what particular trade services should be included in the portfolio that would consitute their "trading company."

   - Assist in the development of the trading company to the point where it is operating successfully.

3. Services for those who want to establish a new company that will participate in the global arena from the day it is founded:

   - The full range of development services, from the feasibility studies through strategic planning until the company is in operation.

Global Trade Services is taking some innovative approaches in its methodology:

- During the analysis and diagnostic stages, we develop the necessary national, regional, or global perspectives of the customers needs, competition, and other aspects of the infrastructure of the business

- We define the critical value-adding activities of the firm to help them allocate resources to the most important activities, and also help them determine which activities can best be done by others.

- While the strategic plan is being developed, it is oriented toward global competitiveness (even though the company may not be able to enter many foreign markets for some time).

- Part of the stragic plan involves the development of the in-company infrastructure required to support international operations.

- During the implementation of the plan for entering foreign markets, we serve as an "expert facilitator" of the support services required to conduct business in each market (including the identification of agents and distributors, establishment of offices, selection of local suppliers, facilities and/or site selection, technical, management and cultural training, government relations, and othr services such as banking, legal, accounting, taxation, quality control, shipping and warehousing)

For companies that are too small to afford the regular services, we are in the process of developing pre-trade seminars which can be tailored either for the management of a small company or for representatives of a variety of companies. These seminars will deal with what is required to become involved in international business.

Chronology of my Experience in International Trade

Prior to becoming involved in international operations in 1966, I had worked for eight years with the Westinghouse Electric Corporation in industrial relations, financial planning and control, production planning and inventory control, and logistics management. My Westinghouse years were split between its corporate headquarters in Pittsburgh, Pennsylvania and the Portable Appliance Division in Mansfield, Ohio.

I joined the Singer Company in 1964 as the Director of Business Planning for the U.S. Consumer Products Division, then became the Assistant Director of Corporate Planning late in 1965. Late in 1966, I entered Singer's international operations. The following is a listing of the internationally related positions I have held since then:

- Director of Planning and Development, Far East Division (South Asia, East Asia, and Oceania)
- Product Manager - Sewing Products, International Group. In that positon, I was responsibible for the sewing product line for 40 subsidiary companies, supplied by 26 sewing factories throughout the world. For thsoe five years, I travelled about 200,000 miles each year through those territories included in the Internatinal Group (the world except for the U.S. Europe and Canada).
- Regional Marketing Director - Latin America North Region (located in Caracas, Venezuela)
- General Manager, Puerto Rico, Haiti, Dominican Republic and Virgin Islands (a $6 million subsidiary)
- Director of Marketing and Planning, Industrial Products Group (a $500 million group of ten company divisions in various industrial products businesses, ranging from gas meters and regulators to industrial sewing machines).

In 1976 I joined the Sunbeam Corporation, where I had two major positions over the next six years:

- Managing Director, Sunbeam Electric Limited (United Kingdom), a $25 million subsidiary with headquarters in England and a factory in Scotland.
- Vice President, Marketing and Planning, International Group. Sunbeam's International Group managed a $700 million business with 27 subsidiaries outside the U.S.

In 1982, I joined Sears World Trade at its inception, and held two officer positions during the next three years:

- Vice President, Marketing and Trading
- Vice President, Business Development, North America.

In 1985, I set up my own company, Global Trade Services, which I have described earlier.

During my years in international trade, I have worked in 60 countries and lived and worked in Venezuela, Puerto Rico and England. For many of my years in international business, I travelled up to 200,000 miles per year, much of it in international marketing where I learned what is required to satisfy customers throughout the world, and to compete effectively against the best global competitors. I have served as the managing director for a $6 million company and a $25 million company in overseas markets, as well as having global responsibilities for three major multinational companies. I am now learning what it is to start my own company as a one man business. My pers pectives on the implementation and effectiveness of the Export Trading Company Act of 1982 are based on my experiences.

Apart from the positions I have held, I have had to speak to a variety of public and private sector groups over the past few years andd therefore have discussed the issues of exporting with the following groups:

- National Association of Cities (1983 and 1984)
- U.S. Conference of Mayors (1983)
- Rocky Mountain Export Council (World Trade Day 1984)
- Southern California Foreign Trade Association (1983)
- Upper Peninsula Forest Products Export Association (1984)
- Smaller Business Association of New England (World Trade Day 1985)
- Export Matchmakers Conference (Chicago - 1985)
- SBIR (Small Business Innovative Research) Program Annual Conference (New York, 1985)

At thsoe conferences, I had very extensive discussions with the particpants and learned of their concerns and successes with exporting.

HAS THE EXPORT TRADING COMPANY ACT ACCOMPLISHED ITS PURPOSES IN THE CREATION AND OPERATION OF BANK AND NON-BANK TRADING COMPANIES?

While it may still be early to detrmine the effectiveness of legislation passed as recently as 1982, my personal opinion is that the results have fallen far short of what was expected when the law was passed.

While I do not have the statistics, my impression is that if one were to measure the amount of export sales flowing through the ETC's developed because of the legislation, these sales would be very small in absolute numbers and certainly very small as a percentage of total exports. In reassessing the Declaration of Purpose stated in the Act, I would say that there has been some progress but if we were to continue to put much hope on this Act to enhance significantly the exports of the U.S., we would be very disappointed. While the Act dealt with several important issues, it falls far short of being a significant catalyst for the growth of U.S. exports.

From my viewpoint, I see bank ETC's closing or cutting back significantly. In some cases, a broader trade services mission has been cut back to dealing only with innovative trade finance, and the international business and trading people brought into the banks have been dismissed. I have continiung contact with various people in bank trading companies and know of their difficulties. In addition to my personal scanning (including discussions with potential clients), I follow the reports prepared by Dick Barovic in his International Trade and Investment newsletter, and it is difficult to find a model of success in either the bank or non-bank ETC's established since 1982.

In a number of cases, I know the ETC's are losing money and I don't know of an ETC that could be used as a model of how to be successful in the business. Admittedly, it may still be early to determine the success of some of these ventures, and we must give sufficient time to meassure their performance. However, one would think that in three years we would begin to see some trading companies on a higher-growth, profitable track. Perhaps I will be enlightened during these hearing by learning of some success models of which I am not aware.

Problems and Barriers to Success of Export Trading Companies

The following problems and barriers to success are based on my own experience in helping in the development of the Sears-First Chicago Trading Company, from discussions with associates who worked for such companies as Fleet Financial, Security Pacific and others. I prefer not to relate specific problems with specific banks or other parent organizations, because the parent organizations are still very much involved in some areas of trade services, and undoubtedly have learned a great deal by some of their mistakes. The following are some of the most significant problems my associates and clients and I have experienced:

- Cultural differences between the parent organization and the "traders" brought into the company to generate trading business. In many cases, the parent organization is not comfortable with the risks involved in certain trading activities, and the parent organization had not identified the types and nature of those risks before they organized the export trading company.
- In many cases there is a definitional problem of what a trader is and what a trading company is. Unless an investor in an ETC really knows what trading is, and has a good understanding of the characteristics of various traders and trading companies, the ETC is off to a rought start. For reference, I have attached as Appendix A a definition of a trader. It is easy to see why institutions like banks and multinational corporations are not comfortable with traders. I hasten to say that a trading company often does not need many "traders," particularly after they have been in business for quite some time and have a lot of regular, ongoing business.
- Little understanding of the "critical mass" required to serve customers in overseas markets.

- No clear mission of the trade services the ETC will provide, products or services in which the ETC will deal, nor of the geographical markets in which it will participate.

- Difficulties in handling a wide variety of opportunities presented to it, particularly where there has not been sufficient time to establish a core of continuing, planned business, or where there has been no definition of the scope of activities and products to be dealt with.

- In many cases, there are too few experienced international business people in the trading company to handle the wide variety and number of opportunities that flow to it.

- The expectations of bank management, multinational corporations and of customers are hard to fulfill.

    - The parent organization management sets the ETC in motion with just an initila concept, and walks away from it in terms of nursing it through its start up, and somehow hope that it will become a success. Within a year or two, the parent becomes impatient and decides it will cut the ETC back or eliminate.

    - Some banks have indicated that the trading company would be spun off because it didn't fit its main stream of activities (a Massachusetts bank).

Types of Resources and Commitment Needed

From the problems and barriers indicated above, one can determine what resources and commitment are requried for ETC's.

- Resources sufficient to provide a critical mass for the services they choose to provide. Let me illustrate:

    - A trading company is not just a trading company. All trading companies are different because they consist of different portfolios of trade services. The trade serice "menu" consists of the following (this list is not meant to be all-inclusive):

        - Brokering
        - Agency representation
        - Distributor
        - Manufacturer/distributor
        - Sourcing
        - Trade finance
        - Project finance
        - Consulting
        - Project management
        - Logistic/freight forwarding
        - Insurance
        - Development of new int'l businesses
        - Countertrade
        - Venture capitalist
        - Merchant of used equipment
        - Importer
        - Exporter (with all the value-adding activities that entails)

    - Whatever the portfolio of trade service the ETC elects to provide, it must put together the critical mass needed to satisfy its customers in its chosen markets and to be competitive in those markets. In fact, An ETC has three customers (1) the supplying company it represents, (2) the distributor/dealer/contractor/manufacturer in the overseas market and (3) the end user of the product or service. If you have only a few people in the ETC trying to serve the needs of U.S suppliers in a wide variety of markets and in a wide variety of businesses, you are not going to satisfy customer needs in a country like Malaysia competing against a company in Malaysia which is an "insider" in that market with a full "business system" to satisfy their customers' needs.

  . The resources required for this "critical mass" will vary depending on what the ETC wants to do, but the resources can be put together either by building that entirely internally, or by establishing an ETC with a minimum of people and network as many of the services as possible. For example, it may have only a few people on their own staff involved in countertrade, and could subcontract their countrtrade work to specialists in various products or geographical areas.

. The commitment required includes:

  . Investment in the necessary critical mass for the services provided.

  . A commitment of time by the investors or the parent organization to plan the enterprise, to clarify its mission, and to provide it with adequate leadership and direction. They must also be prepared to give the time necesary to be involved with the new ETC and its issues, particularly during the difficult early months and years

    . I am consulting now with a corporation which is taking the time to enter the trading company arena judiciously.

  . The patience and long term view necessary to make a success of the ETC.

Key Factors for Success in Trading Companies

The following are some of the key factors for success in export trading companies:

. Clearly defined reasons why the ETC is being established, and with policies and strategies integrated with those of the parent organizationor with thsoe of the investor's other activities.

. Leadership by people experienced in trade and all aspects of international business.

. An international network of associates and associated firms which have product and geographic knowledge and key customer contacts.

- A go/no-go "gatekeeping" capability to decide quickly on pursuit or rejection of new business opportunities so valuable time is not spent on useless activities.

- A realistic chance to build a critical mass of trading voluem rapidly.

- Ability to represent reliable, economical, quality-conscious suppliers.

- Some control over the use of brand names which will prevent suppliers and distributors from "walking away" when they think the ETC is no longer needed.

- A compensation system for traders which will keep them content enough to remain with the ETC.

- Adequate focus on trade services, products and services, and geography.

- A clear ability to provide the full range of international services required by the supplying company, i.e, the ability to act as the international department for a U.S. manufacturer or service company.

- The ability to meet customers' needs in the markets chosen for export, and to compete effectively in those markets. (See Appendix B for the services I believe a full-service ETC should provide for its suppliers, and what the suppliers must do)

- Sementation of its business so the ETC can elicit the suppliers' business on a targeted basis, rather than just having to react to a wide range of opportunities which do not relate to the capabilities of the ETC (recognizing that an ETC must always have an attitude of being alert to the great opportunities that are always emerging).

- Financial strengths, such as the commitment of adequate financial resources, the ability to extend credit, and innovative capabilities to fiannce transactins and investments globally.

- In the domestic market, access to good, marketable products, and a good trade infrastructure, such as offices, export trade documentation, freight forwarding and shipping capabilities, good communications capabilities, banking support, etc.

- In the international trade arena, be knowledgable about the conduct of international trade; have access to international market information, and the ability to gather it, analyze it and quickly formulate actionable positions on problems and opportunities; know foreign currency management; and have an adequate international infrastructure including (1) distribution network and a cusotmer base; (2) logistical capabilities, (3) after-sales service; (4) communications, (5) offices, and (6) good local associates.

Time Required to Develop an ETC

While it is very difficult to determine exactly how long it should take to establish a successful export trading company, the following will serve as a guide, based on my experience:

- To build an ETC from ground zero, it will take at least five years to build an ETC of substance.
- It is possible to do business once there is a plan for the ETC, but it will take months and years to develop a substantial business.
- Acquisition of an existing business can speed the process significantly, but the right acquisition is hard to find.
- A networking approach to acquire certain capabilties can also speed the process of reaching significant volume and attaining profitability.
- It is wise for an ETC to keep a low profile during the start up months so the ETC can control the type of business it gets and the speed with which it must serve it new customers.
- I believe research must be done on the start up experiences of ETC's particularly those started since 1982. The ETC's certified since 1982 would make a good collective case study.

Lessons Learned from Japanese Trading Companies

The following is only a partial list of some of the lessons we can learn from the Japanese trading companies (and not just from the Sogo Shosha):

- They have been successful because of the extensive experience their people have had in international trade. They send their people overseas and give them extended experiences in a number of countries.
- The country itself has had a need for and a dedication to international trade for many years, and it has been a significant share of their GNP for a long time.
- They have been patient in building markets and in expecting results.
- The relationships of trading companies to banks have provided them with access to short and long term credit debt at extremely favorable rates. The Japnese trading companies are always globally competitive in their financing.
- They have excellent worldwide communications networks.
- They do have critical mass for the trade services they provide.

- The group relationship they have with manufacturers and banks allows them to look at the total profitability in manufacturing, finance, marketing and the trade intermediary activities. There is a willingness on the part of the owners of the trading companies to take lower margins than U.S. companies would accpet because of the profits generated in manufacturing and banking.
- The Japanese have a tremendous number of overseas offices. Just counting the overseas offices of the nine Sogo Shosha, there are about 900 overseas offices. While t hose offices serve as communications points and gatherers of market intelligence, they are also able to transact business. Therefore, if a small Japanese company wants to do business in Frankfurt, for example, it can work through one of the Sogo Shosha which have offices there and just choose the one that will best serve its needs. If an American company wants to do busness in Germany through an office in Frankfurt, it can get information in Frankfurt on doing business in Germany, but doesn't have anywhere to turn to help it transact business, unless it searches out some ETC that might have some capabilities in Frankfurt.
- The Japanese have a tremendous market intelligence system with their network of worldwide offices and their system for gathering and disseminating market intelligence.
- They have a very good system for handling new opportunities. They have ongoing core businesses which provide the vast majority of their revenues, then have a very good system for handling the small percentage of their business that is new. While their entire organization is open to discuss new ventures, those new opportunities are channeled very carefully to a select few people with experience enough to judge the viability of those opportunities.
- They have a strong base of domestic business that provides them with economies of scale as an advantage in their international business.
- They are provided with incentives for investing in building international markets.
- They work in the national interest of the countries in which they do business.
- The specialized trading companies of Japan are more profitable than the large general trading companies.
- They handle commodities and undifferentiated products very well, but don't do quite so well at selling specialized and technical products (this comment applies to the Sogo Shosha)
- The profitability of the Sogo Shosha are unacceptably low for American companies, and therefore it is not wise just to emulate those companies.
- The Sogo Shosha may be too large to continue to be effective.

Commerce Department Support/Promotion of Export Trading Companies

Beyond the initial push provided during the 1982-1983 period when the Department took its story to various groups throughout the country, I have not seen much high visibility support of ETC's by the Commerce Department. I have seen the literature prepared by Commerce and know that they are supporting ETC's from their various offices. This is not meant as a criticism, but the reality of trying to get the message out with modest resources. When I have spoken at various conferences, Commerce is represented and does tell the story. From my vantage point, that of one individual in the trade services field, I am aware of the Department and its ETC activities, but believe the impact while important is modest.

In terms of the guidance provided by the Department of Commerce to ETC's, I am not aware of significant guidance being provided. In fact, there are probably relatively few people in the Department who have actually worked for or managed an ETC, particularly during the start up of an ETC. Therefore, there are few people who can provide guidance from their own experience. The people who could provide guidance to new ETC's are probably very busy running their own ETC's or are international business people who are well paid for what they are doing today and have little time to give providing counsel to new ETC's.

The suggestons and recommendations regarding the issues of support and promotion of export trading companies will be co vered in the next section of this report.

HOW COULD THE ACT BE IMPLEMENTED MORE EFFECTIVELY/OTHER LEGISLATIVE CHANGES PROPOSED

While it is always possible to improve the implementation of legislation, I doubt there will be very good returns from great efforts to improve this legislation and its implementation. While bank participation in trading companies and antitrust protection are important isues, legislation dealing only with these issues misses confrontation with the larger issues involved in the crisis we are now facing.

Improved implementation of the ETC Act will hardly put a dent in our trade deficit of $148 billion. Concentration on the ETC Act may actually be a diversion keeping us from dealing with our crisis.

I believe our trade deficit of $148 billion in 1985 and $16.5 billion in January 1986 brings into focus a national crisis regarding the export effectiveness of our country and our inability to compete against foreign made goods and services. Our companies are losing their global competitiveness.

I believe we need a "Manhattan Project" to deal with this crisis. Somehow we must muster our forces as we have in times of other national crises and recognize that we are engaged in international trade warfare and we are losing.

There are those who say that the problem is not with exports, that exports are increasing. They say that our problem is with imports. Those people tend to lull us to sleep so that if we just increase our exports slightly each year that will be alright. Unfortunately, we do have a problem with exports. In expanded world trade, we are going to have to have a much greater share of our GNP in exports if we are to afford the luxury of a high level of imports.

There are also those who say that the high level of imports are acceptable because of the benefit that provides to the debtor nations in pulling them out of their problems. Despite the very high surpluses the debtor nations had with us in 1985, that did not really solve their problems, so we can't just let us feel that our trade deficits with those countries is a good thing.

Other say that the export situation will get much better now that the dollar is softening, and now that oil prices are declining. The January deficit should give those people cause to reasess their views. While exports of commodities might change easily with a change in the value of the dollar, the supplying sources for consumer products and capital goods have largely shifted overseas and the factories in which those products were made are now closed and their workers have gone elsewhere.

Companies that closed U.S. factories and opened new factories overseas, or out-sourced their complete products or components are not likely to reverse that process in the near future.

We need a unified focus on and commitment to enhancing the export effectiveness and global competitiveness of U.S. business, both manufacturing and service companies, and improved implementation of the ETC Act, while desirable, will not begin to touch the problems.

I concur with those who favor the consolidation of the federal government's trade adminstration. As difficult as that may be, our trade crisis demands it at this time. Will it take a $200 billion deficit, and then a $300 billion trade deficit for us to act?

We need statements from the highest levels of government that exporting is a top priority for our country. It will avail us little if we have regained our military strength but have our economic muscle atrophy. Our solution to the trade deficit cannot be protectionism, it must be enhanced exports.

The "Manhattan Project" I propose would best be initiated by a task force with several working groups to determine what must be done to resolve the country's weakening position in international trade. Some of the issues which must be addressed urgently and then incorporated into legislation include the following:

- Pre-trade advisory services for smaller companies that are affordable.
- The need for overseas offices of some sort to facilitate actual transactions.
- Getting the knowledge of export services and export trading companies to the small to medium sized companies often enough

to get through to them.

- Assistance in feasibility studies and other funding required to get firms to an international condition.
- Coordination of the many organizations now involved in the export effort. There are great efforts being expended by states, regions, cities, port authoriities, trade associations, world trade centers, export clubs and others and each has an important role to play, however, that information on thsoe activities is so fragmented that there is little impact on those who need the help. A database of these participants that could be accessed inexpensively by small to medium sized companies is worthy of consideration.
- Examination of current data bases of international trade information and who uses it and how.
- Research into current experiences of export trading companies and smaller new to export companies would be revealing and could provide new insights into how exporting could be enhanced. Universities may be well-equipped to undertake such research (I have made this proposal to several universities, but the interest was not sufficiently high to undertake such research in 1985)
- Consideration of incentives for exporting or for import substitution.
- Consideration of incentives for those who set up ETC's.
- Examination of impediments to our abilities to export and to combine to combat foreing competition (while maintaining the proper safeguards in the antitrust area)
- Incentives for major capital investments aimed at import subsititution and global competitiveness.
- Examination of the capabilities of some of our institutions to deal with global competitiveness (for example, the work being done at the International Trade Commission to assess global industry competitiveness is excellent as a format for companies to use in assessing their own global competitiveness).

These are only a few of the issues which such a task force could address in leading to some recommendations for to deal with our need for increased export effectiveness and global competitiveness of our industries and our services.

Such a task force shoudl be made up of those who have had significant experience in international trade, but not empahsizing larger corporation experiences. There should be representation of thsoe who know the realities of small to medium sized businesses and what issues they face in expanding to an international condition.

While a blend of experienced people from the public and private sector is desirable, the voices of those who have had to deal face to face with the realities of international trade and who have had to earn a profit in that arena with scant resoruces should be well represented.

I do not suggest that we should not try to improve the effectiveness of the ETC ACt of 1982, I do strongly urge that we go beyond the scope of that legislation to deal with the crisis we face with our trade eficit in 1986.

I sincerely hope that my observations may be useful to you in conjunction with those of my knowlegeable and experienced colleagues.

APPENDIX A

DEFINITION OF TERMS

It may seems rather elementary to put a lot of emphasis on the definition of trading terminology, but in my experience in the world of traders and trading companies, the lack of understanding of semantics causes immense problems, thus my very strong feeling that we all agree on what we mean by certain words. For those who are interested, I will be glad to illustrate some examples of the problems I have experienced first-hand.

TRADE

The dictionary definition of "trade" is:

> "The buying and selling or exchanging of commodities either by whole or by retail within a country or between countries, i.e, domestic trade or foreign trade."

I have emphasized domestic trade, because there are those who overlook the importance of domestic trade in constructing trading companies. While it may be appropriate for certain specialized trading companies to avoid domestic trade, the larger trading companies of the world have strong roots in the domestic market, for the strength that gives them in international, i.e., foreign trade.

TRADER

While there may be some misunderstandings about what is meant by "trade," there are enormous differences in people's perceptions about what a "trader" is. The following is my own definition:

. A trader is one who knows enough about the business infrastructure of a commodity or product to:

  . Locate suppliers then buy the products

  .. Locate customers and sell the merchandise

  . Coordinate all the activities required to move the goods from supplier to customer

  . Find the money to support the transaction

  . Negotiate with shipping companies, insurance companies and any others involved in providing trade services

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- Judge the creditworthiness of customers

- A trader may trade in a variety of commodities or merchandise, but they will differ greatly in their dexterity in handling different goods.

While this definition can stand on its own, it is well to qualify the latter aspect of this definition, then proceed to describe some of the characteristics of a trader.

Traders differ greatly in their degree of dexterity in handling a variety of goods. Some traders confine themselves to a narrow product line. Others branch our into related commodities or similar **semifinished** goods. Still others deal in any goods, services or technology they think will be profitable.

There are no hard and fast rules as to how far a trader can diversify. Generally, traders in bulk commodities move into other bulk commodities before trying intermediate and finished goods (from cotton into greige goods then into textiles, for example).

Traders in finished goods are contrained by the complexity of the products they propose to buy and sell. The more complex the product, the harder it will be to compete with traders who specialize in that complex product, and the harder it will be to compete with manufacturers of the product who sell the product directly.

For people who have not been involved in various businesses throughout the world, they may not appreciate how difficult it is to move from bulk commodities to consumer goods to telecommunications, for example. While a trader in cotton may be able to handle most aspects of a transaction in cotton (though that trader will be better off with a good "back room" to handle the details of the transaction), one who calls himself a trader in consumer durable products could never begin to handle the selling, servicing and other support activities involved in consumer durables businesses alone.

Characteristics of Traders

The following are important to understand about traders:

- They understand very well the risks and rewards associated with their trading

- A really good trader knows the worldwide business infrastructure of his business

- A trader knows where his commodities or merchandise are produced, processed or grown, and knows the costs to produce the goods and to land those in the key markets of the world

APPENDIX A

- A trader knows the world trade flows for his products.
- A trader knows the customers needs, key markets and channels of distribution
- A trader personally has developed sources of supply for the products and personally has marketed to and sold his products. The better traders have a stable of long time loyal customers who will follow him wherever he goes.
- A trader knows important competitors throughout the world sufficiently well that he can anticipate many of their moves
- A trader knows what factors affect the future of his business and monitors those very carefully
- The trader knows the principal information sources for his business, and also has an informal "early warning system" to alert him to significant developments
- A trader has a network of people who help to generate leads for him, and to provide support in getting deals accomplished
- A trader often is involved in a variety of ventures, because he likes to get involved in what he anticipates may be profitable deals, and because he is free to become involved
- A good trader can size up business opportunities very quickly, and can also size up people very quickly. That ability is vital to a trader's success. He may be involved in putting together three mini-ventures in the same day.
- A trader is not likely to be constrained by the rules and pay structures of corporations. This is one of the major problems in trying to put some traders into a corporate structure. A good trader is probably making several hundred thousand dollars and thinks he can make a million - and occasionally does. He always wants to feel he can make a million with the right deal, and doesn't want to think some corporation might prevent him from making the "big deal of his life."
- A trader makes a living on brokering fees, commissions, on margins earned when he risks taking title, by having a partial ownership in a new venture, or by finding any possible way to make money that his imagination might discover.

These are the characteristics of individual, entrepreneurial traders. We shall see that there are relatively few real traders in a trading company, even though there is a trading mentality.

Myron M. Miller
August 1985

APPENDIX B

VALUE ADDING TRADE ACTIVITIES

MARKETING:

PRODUCER OF PRODUCT OR SERVICE	FULL SERVICE EMC/ETC
. Global market assessment to determine priority countries and products, and to identify key competitors	
. Joint preparation of marketing plans for each country	. Joint preparation of marketing plan for each country
. Provide continuous flow of new products	. Provide extensive knowledge of the local market, its culture, languages, tastes, trends, etc. to assist supplier in development of appropriate products or services, product features, styling, packaging and advertising
. Preparation of product literature in languages required	. Provide translation services if it can be done more accurately and economically within a country
. Preparation of advertising and sales display materials	. Provide input on unique requirements for local markets, assist in translation, print locally
. Provide sales training and service training materials	. Translate sales and service training materials. Conduct systematic sales and service training in new and existing products or services.
. Visit the market periodically, gather data, visit customers, distributors, stores, etc. to understand the market and to share those views with the distributors and agents.	. Provide market data to the supplier based on systematic monitoring of the market and competition
. Bring distributor personnel, retail personnel, agents and other key overseas people to supplier's headquarters (and factories) for training	
. Devise best methods to provide spare parts or other types of customer service in timely, economic ways	. Provide after-sales service for the products or services, in the shortest possible time. This usually requires stocking sufficient high mortality parts to insure a high degree of customer service.
. Develop prototype sales promotion materials for use in international markets	. Provide sales promotion assistance by implementing a sales promotion devised by the supplier or a sales promotion developed locally suitable for the local market
	. Implement the marketing philosophies and strategies of the supplier
	. Serve as a conduit of new ideas, new concepts, and new product concepts from supplier to end user and vice versa

PRODUCER OF PRODUCT OR SERVICE	FULL SERVICE EMC/ETC
MARKETING:	
	. Provide broad market coverage for the supplier by making regular contact with the greatest possible number of end users (for consumer products, reaching the greatest possible number of retail customers and retail outlets)
	. (For consumer products) When products require demonstration to the ultimate customer, provide that demonstration capability in a manner equal to or better than that of competitors. (This also applies to commercial products businesses)
	. (For consumer products) Assist dealers with constant training of store personnel in product benefits and how to sell those products, to gain competitive advantage.
FINANCE:	
. Develop adequate capacities for understanding international finance, including the development of skills for dealing with countertrade, foreign exchange management, overseas banking, international flow of funds, sources of funds, etc.	. Purchase the products from the supplier domestically and handle all aspects of international trade and project finance.
. Understand government assisted financing at the federal, state and local levels.	
. Develop familiarity with special financial arrangements in other important parts of the world, including governmental assistance, special benefits provided, etc.	
	. Provide competitive financing in each market, consistent with the ability of customers to pay promptly.
	. Where dealers are involved, help them be profitable, even running seminars teaching them the financial management of their business
	. Develop policies and methods for insuring effective cash management, and the management of inventories and receivables
PRODUCT PLANNING AND DEVELOPMENT/ RESEARCH AND DEVELOPMENT:	
. Design products suitable for international markets	. Provide marketing information on local product requirements

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PRODUCER OF PRODUCT OR SERVICE	FULL SERVICE EMC/ETC
PRODUCT PLANNING AND DEVELOPMENT/ RESEARCH AND DEVELOPMENT:	
. Provide the necessary research and development to maintain product leadership and provide unique competitive advantages	. Provide information on competitive products in each country, especially on new products
. Understand worldwide technical requirements for government approvals, so products can be designed to those specifications. Take lead in obtaining special approvals.	. Assist in obtaining local government standards approvals
. Maintain system for evaluating competitive products and services from principal competitors throughout the world, to assure competitive leadership	
MANUFACTURING:	
. Provide products at globally competitive costs, so the products may be priced competitively in the marketplace.	
Provide highest possible degree of product quality and reliability (may require periodic quality audits in the market place, plus an early warning system to provide feedback from each country regarding existing or potential problems.	. Cooperate with supplier in providing quality audit information or other "early warning" information that can help the supplier correct quality problems as quickly as possible.
LOGISTICS:	
. Ship products on time; ship complete orders, not partial shipments, whenever possible	. Where product are taken from the domestic supplier, ship products on time and ship complete orders, not partial orders
. Provide completely integrated computerized international trade documentation system. Insure that documentation is accurate	. Where goods are taken from the supplier domestically, provide computerized international trade documentation system, incorporating not only its needs but the supplier's needs
. Establish sales forecasting/feedback system to ensure that products are produced and shipped in an orderly manner, so that inventories are minimized for the supplier, EMC/ETC and the overseas distributor.	. Provide accurate sales forecasts to supplier for optimum inventory management
. Maintain a safety stock inventory of high volume products and parts	. Maintain sufficient inventory of products and parts to provide a very high degree of customer service
. Provide efficient inland transportation from factory to port of shipment.	. Provide ability to ship goods overseas at the lowest possible costs, in the shortest time.

PRODUCER OF PRODUCT OR SERVICE	FULL SERVICE EMC/EMC
LOGISTICS:	
	. Arrange freight forwarding, cargo space reservations, transit insurance, packaging, warehousing, customs documentation and inland freight.
	. Efficient transportation to the customer within each country.
	. Provide information to the supplier regarding the things the supplier must do to assist in making the logistics processes as efficient as possible
LEGAL:	
. Screen foreign distributors for compliance with U. S. regulations	. Comply with U.S. and local legal requirements in all areas

APPENDIX B

Myron M. Miller
August 1985

CHECKLIST FOR EVALUATING EMC's AND ETC's

- Who are the existing clients of the EMC/ETC?
- What experience does it have in the countries you are interested in?
- What experience does it have in your products or services?
- What is is "critical" mass to serve you in various countries, i.e, what services is it capable of performing for you in each country, and how many clients does it have in each country?
- Get names of other clients of the EMC/ETC so you can determine the satisfaction of these clients?
- Exactly what services does it perform for its existing customers and what services can it perform for you?
- By what criteria does it select distributors in various countries?
- How long has the company been in business?
- For how many years has it represented various companies?
- What value-adding functions does it perform itself, and which does it subcontract? To whom does it subcontract various services?
  - Go through a checklist, function by function, to identify the services the EMC/ETC can provide
- What is the sales and profitability growth for it customers?
- What is the organization of the EMC/ETC, where are their people located, what are their responsibilities?
- Visit the offices of the EMC/ETC to assess the company in operation. Look at the international trade documentation capability, for example. Talk to the key marketing people to discuss what they do in key markets for their clients.
- What are the plans for the EMC/ETC for the next few years?
- If you became a client of the EMC/ETC tomorrow, do they have the capacity to handle your business on top of what they already have?
- Does the EMC/ETC handle the business of one of your competitors?
- What customers has the EMC/ETC lost in the last three years, and why?
- Personal profiles of the key people in the firm. i.e, how many years in what kinds of international operations?
- What characteristics distinguish this EMC/ETC from others?
- Is the firm in other businesses?

Mr. **Barnard**. Thank you very much, Mr. Miller.

Mr. Chew, in your testimony you focus on export management companies, and I'll be honest with you, I'm not that familiar with them. What is an export management company?

Mr. **Chew**. Mr. Chairman, the nomenclature in my industry is infuriating because most of it was invented in Washington by people who don't know anything about our business.

Mr. **Barnard**. We'll give you an opportunity right now to tell us.

Mr. **Chew**. There is no difference between an export management company and an export trading company, none whatsoever. When Congress thought they were inventing something new, there had been successful export companies in the United States for many, many years.

We call ourselves exporters; during the fifties, the Commerce Department decided to calls us export management companies, now we are also called export trading companies; but there is not a single particle of difference. You can debate this all night. Many people have different definitions, but functionally, when the legislation was passed, I changed my letterhead—it had said "Export management since 1915"—to now read "Export trading company, export management since 1915."

Export management companies usually represent American manufacturers on an exclusive basis for overseas sales; they may also be nonexclusive sales reps. Many do countertrade. There is no functional difference between export management companies and export trading companies.

Mr. **Barnard**. Can you explain why export management companies or export trading companies were ignored from this act?

Mr. **Chew**. The legislative history of the 1982 bill was a bit of a mystery. I think it came out of some Congressman's assistants who thought they would do something about exports, and I think the banks were surprised, just as we were. I don't think the banks regarded it as a great opportunity, and they supported it nominally.

The banks did not really make a serious effort to make the legislation work. They just accepted it, I think, from the point of view that it was presented as a kind of deregulation of banking.

From our side, in our industry, it was an enormous lost opportunity, and the banks' very casual attitude toward this was a dereliction of public responsibility, as far as I'm concerned. They supported it through the Bankers for Foreign Trade [BAFT], but made no effort to make the legislation functional.

That's a rather strong point of view, but that's what I feel. It was a tremendous lost opportunity, and if the Congress does it again in 1986, it will be a tragedy.

Mr. **Barnard**. Mr. Miller, in your statement you said that there was somewhat of a natural conflict between bankers and traders. But really, wasn't the purpose of this act to put them together—that here is a group of people in our country who are expert in their field, and they are traders, and that we were putting this bill together in order that they would maybe have the advantage of financing from the banks? Is that just an abnormal combination?

Mr. **Miller**. With all respect to my banking friends, I think it is an unnatural combination.

Let me modify this statement. As far as the trade finance service and some of the other trade services that I mentioned earlier when I discussed the "menu" of services, there are certain trade services where there clearly is an enhancement between banks and traders, however, concerning the other types of trade services which have to do with the marketing aspects of the business, of actually getting out and selling to customers, taking risks, finding customers and putting deals together—the inclination of the trader is to take on a much greater degree of risk than banks are generally comfortable with.

Mr. BARNARD. For the sake of time this morning, I'm not going to go in great detail—I wish I had time to do this, Mr. Chew—on your proposal. But since it's part of the record, I'm going to assure you that those proposals will be in the record, which will be shared with any legislative committee; I can assure you of that; it could be considered in a new bill in the House. I would strongly recommend that Senator Heinz, in his consideration of his bill, likewise consider these proposals.

Mr. CHEW. I handed him a copy of my testimony with the Touche Ross article containing my proposals attached, when he went out the door.

Mr. BARNARD. I think that was excellent.

I think we have covered most of the things which I had that I was wanting to bring up. I might say that we certainly do appreciate the testimony of Mr. Hammonds in his experience with the Eximbank. This particular testimony came in late as far as our consideration was concerned, and we did not have an opportunity to invite the Export-Import Bank to be present and to discuss their role in the financing of ETC's, but we will be giving them an opportunity to provide information, discuss their role, and answer some of the questions that Mr. Hammonds has raised. [See app. 6.]

Mr. Kolter.

Mr. KOLTER. Thank you, Mr. Chairman.

I think the panel was most enlightening. I just wanted to ask Mr. Chew a question relative to your first question, Mr. Chairman, as to ETC's and EMC's.

Does that present a problem to the Japanese at all? Do they have any problems with their EMC's and ETC's and what stands for what over there?

Mr. CHEW. The Japanese trading companies have been around a long, long time, and as described by my associates here, they perform a great many functions, not just export. As a matter of fact, exporting Japanese goods is a small part of what they do. But there are 7,000 Japanese trading companies, most of them are engaged in export and are part of Japan's export success.

In our country I do think that the nomenclature, as the chairman has implied, is very confusing. It has deterred people from really getting an understanding of our industry. A better understanding of our industry is, we think, a very important means to increase American exports.

I get tired of explaining the alleged differences between an export management company and an export trading company, when there are no differences. All export management companies do much of their business, as Mr. Hammonds described, financing, taking credit risks and taking title, just as trading companies do in Japan. It's a very important part of our function.

I think one of the original concepts of the legislation was that if banks in the United States, which had not traditionally been very active in trade finance, were allowed to have an equity position, they would become better financers of American exports; they would finance the exports of smaller companies; and they would innovate the new devices for trade finance. None of this has happened. I think this was a misconception in the original legislation.

This is one hell of an assignment to give you gentlemen, but we have a real trade crisis in this country, and export management companies are a very efficient way of focusing on the export side of the balance of trade because of our export-related efficiencies and economies.

Mr. **Kolter**. The point I was trying to make, all these brevities and names seem to add more confusion to an already confused Congress.

Mr. **Chew**. No question. It's been bad for the industry and bad with respect to the ability of Congress to focus on the real issues facing our industry. From Congress' point of view, from the point of view of the industry, there's no difference between an export management company and an export trading company; they're both export companies, and they both would benefit from the kind of programs that we propose.

Mr. **Kolter**. Mr. Miller, you mentioned the Japanese. As long as I've been down here, everybody we talk to, they seem to be superpeople—superhuman people. You mentioned that the Japanese can go to Frankfurt, open up nine companies; they can train their personnel, and so on and so forth. My question to you, since you seem to have some knowledge about these people—who pays for all this over there? Who underwrites the cost of this type venture, including training, and so on and so forth, compared to what we do here in these United States?

Mr. **Miller**. Let me start by mentioning, as Ralph Chew also mentioned, that the Japanese trading companies have been around for 100 years. So they have quite a history—a history that was really enhanced in a unique way, because Japan is a country with few natural resources. The trading companies had to bring all the raw materials into Japan, and then after the goods were processed, they had the responsibility for marketing it not only overseas but also in Japan.

As Ralph properly pointed out, only about 20 percent of the revenues of the major trading companies are exports. These companies have total revenues between $60 billion and $80 billion. Just under half of that, in many cases, is domestic sales in Japan. A company like C. Itoh has 250 subsidiaries in Japan involved in wholesaling. Most of these companies have a very strong domestic base, and maybe about 20 percent or so of their sales are exports; then there are imports and third-country trade.

But over a period of years there just has been a commitment to the unique role of trading companies in Japan, as trade intermediaries and generators of trade. There were, in a sense, specialty manufacturers, and the trading companies handled the rest of the trade services. They were able to finance themselves—with bank support—throughout the years until they are now gigantic companies. They didn't get that big quickly.

Mr. **Kolter**. Well, the initial money did not come from the government, did they, or from the banks? Where would they come from? From their own personal accounts? For example, a man like Mr. Hammonds, if he were Japanese, would he have any problem getting started, if he were in Japan, for example?

Mr. **Chew**. Mr. Kolter, could I comment on that? I'm interrupting my friend. Japan has these well-established 100-year-old export trading companies that do billions of dollars around the world and have thousands and tens of thousands of employees. Yet about 60 percent of the exports of Japan are Government-subsidized.

Mr. **Kolter**. That's what I was waiting to hear.

Mr. **Chew**. The United States—the Eximbank is involved in less than 5 percent of our exports. World commerce, unfortunately, reguires the involvement of government. Our Nation's prejudices are very much against this; we believe in a market economy. But when you are doing business country to country, both Governments are going to get involved. An air of realism should come into this. Everybody else is playing the game this way, and for the United States to step back and say, "No; we're holier than thou; we believe in a market economy"—which we do—"in the world market," is simply going to continue the present disaster.

Pardon me for interrupting.

Mr. **Kolter**. Mr. Chew, thank you for your honesty. What I was looking for was the fact that there was subsidy from the Government there, and in Mr. Miller's testimony he is relying here, he says, on the private sector. So again we're not comparing apples with apples and pears with pears.

Mr. **Miller**. When I say we must rely on the private sector, this is not to say that a real examination of some basics is not in order. It's not for me to say what legislation we can provide to enhance exports, but I think we need to examine what the Japanese are able to accomplish and then find out what we can legislate to provide incentives or some other measures to enhance exports. How far can we go legislatively? The Government still has to be a critical partner.

Mr. **Kolter**. But you have to admit, it's pretty difficult to compete against a government.

Mr. Hammonds, I'm sorry I didn't get an opportunity to meet you much before the hearing this morning, but the question I have in the back of my mind is this. When you finally got started, did you get started with local Butler County money, or did you go elsewhere for the banking assistance?

Mr. **Hammonds**. I started with local Butler County money, right at the local Mellon branch office. But then I had to collateralize the loans that I got with personal assets. I might say that I have had some extensive experience in dealing with banks. I think now I've dealt with four different banks in trade finance just on a loan basis. I also approached two of the bank ETC's that were formed about the possibility of financing some of our trade transactions, neither one of which was interested. At the time of the approach, we had loan facilities with both of those banks, with the parent bank, and they weren't interested.

Mr. **Kolter**. Mr. Hammonds, we're really impressed with what you are trying to do; I just want you to remember that. I talked with Senator Heinz this morning. He and I are most interested in helping you out, and if our offices can be of any further help to you, please utilize us.

Mr. **Hammonds**. They really have been, Mr. Kolter, and Mr. Heinz' office—in fact, I don't believe that I would have ever received the meeting with the Chairman of the Eximbank had it not been for Senator Heinz' office calling. As my colleagues here say, this is a crisis that we're facing, and it is time we do something about it, and the fact this committee is meeting encourages us sitting out here anyway.

Mr. **Kolter**. Thank you.

Thank you, Mr. Chairman.

Mr. **Barnard**. I have two very brief questions.

Mr. Chew, do the EMC's need the antitrust protections that are in the ETC bill?

Mr. **Chew**. Most of them in most circumstances probably do not, sir. I did make an informal survey of the industry when I received your letter, and I asked the former president of the California group if he knew whether his members had been certified and he said no. I have seen the list of companies that have asked for certification and recognize none on the list as experienced EMC's.

But certification might be of possible future use to our company. We have a couple of projects with manufacturers where we might come for certification. All of us can imagine consortia of contractors and engineers getting together on a project and so forth. But it's not a very important consideration, sir.

Mr. **Barnard**. We just haven't moved that far in our trading experiences, have we?

Mr. **Chew**. Frankly, in our perception, most of the business we do does not have antitrust implications. We are an arm's-length buyer of products from many companies. If those companies compete, we're not colluding on price with them because it wouldn't further our business. The perception that the Antitrust Act is enormously inhibiting to exporters is not correct.

Mr. **Barnard**. Mr. Miller, does the Export Trading Company Act offer certain protections and benefits to the ETC's that are not offered to EMC's? Or Mr. Chew—either one.

Mr. **Chew**. No. Of course there is the specific question of banks being certified, but that's a separate function you are not directing your question at. I cannot see that there would be different benefits for ETC's or EMC's. Again, I insist that they are both the same animal.

Mr. **Miller**. I concur with that.

Mr. **Barnard**. Gentlemen, we appreciate very much your testimony and the contribution you have made to these hearings. I think it's going to be very helpful in developing the record for the further consideration of future legislation.

Again, I appreciate your suggestions as far as the legislation is concerned, and I'm sure they are going to be considered.

Mr. **Chew**. Thank you very much.

Mr. **Barnard**. Thank you very much.

[SUBCOMMITTEE NOTE: The following statement was submitted by the Council for Export Trading Companies for inclusion in the record:]

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REVITALIZING THE "YANKEE TRADER"

submitted to;

The Commerce, Consumer,& Monetary
Affairs Subcommittee.
Chairman. Rep.Doug Barnard. Jr.
United States House of Representatives

prepared by;

Ronald C. Wakeford
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Revitalizing the "Yankee Trader"

Increasing exports through the use of export intermediaries has long been recognized as a desirable method of reducing trade deficits. Historically, and before the birth of the present-day multinationals, U.S. trading companies held their own in world commerce and accounted for a sizable fraction of American exports. Between World Wars I and II, and coincident with the international expansion of major U.S. corporations, the independent "Yankee Trader" began to account for a much smaller fraction of national exports.

Today, independent trading companies export less than 10 percent of U.S. goods and services. Without increased national recognition and support for these entities, even this small fraction may see further erosion. The need for capital development, new tax incentives, a national information system on export markets, and other supportive efforts is readily apparent. Present reliance upon international divisions of major corporations to close the trade gap is a short-term solution. A national strategy to serve the long-term interests of global trade must be devised.

The ETC Option

In 1982, the Export Trading Company Act (ETCA) passed both houses of Congress unanimously, vigorously supported by the Administration, after an evolution of almost four years. Conceived in response to successful Japanese and European trading institutions, the act was designed to encourage development of new U.S. exporting entities. Several major factors led to the enactment of this legislation:

- Small and medium-sized businesses were virtually nonparticipants in the export field. It was felt they needed umbrella organizations to stimulate trade activity.
- Existing trade intermediaries of any size were few in number, lacked equity capital, and accounted for only a fraction of U.S. exports.
- Antitrust immunity was needed to reduce legal impediments and thus encourage businesses to undertake joint ventures overseas.

By mid-1985, some ninety institutions had received approval from either the Federal Reserve Board or the Department of Commerce (DOC) to invest in, or commence operations as, export trading companies (ETCs). Among the ninety were thirty-eight formed by the banking industry; the balance received export trade certificates of review from DOC. These two distinct groups of newly established traders continue to evolve, although the pace of development is considered slow by many.

The reasons for this apparent slowness in reacting to the ETC option are complex. However, the conventional wisdom that identifies the strong dollar, the budget deficit, and foreign import constraints as the culprits provides only a partial explanation. Other problems, including structural and informational weaknesses in the U.S. approach to trade, may be even more important. Some of these difficulties may be illustrated by discussing the obstacles confronting ETCs as they attempt to penetrate world markets.

Obstacles Confronting ETCs

Bank Holding Company ETCs One of the most significant problems facing U.S. trade intermediaries is the shortage of equity capital. This fact was discussed repeatedly during hearings on the ETCA. One result of these deliberations was the deregulation of the banking industry to allow equity participation in the establishment of trading companies. It was anticipated that, in the main, banks would form partnerships with manufacturers or other trade intermediaries to venture jointly into the exporting field. This has not happened. The overwhelming majority of bank holding company ETCs (BHC–ETCs) are wholly owned subsidiaries of the parent organization. Attaining the desirable mix of financial skills, exportable products, trading know-how, and equity capital generally has not proved possible. There are, of course, exceptions, such as Valley National and Society Corp., and the hoped-for trend is now developing among regional BHCs.

Several problems stem from the regulations governing qualification as an ETC, which require that revenues be principally from exporting as opposed to importing or other nonexport–import activities. This requirement ignores the total volume of goods traded, and can result in a distorted picture of the results. For example, assume that $5 million worth of goods are exported and a 10 percent profit ($500,000 revenue) realized; on the other side of the equation, imports amount to $8 million with revenues of 6 percent ($480,000). The principal test has then been met. However, in this instance the ratio of exports to imports makes for a continuing trade imbalance. Clearly, the regulations need further review to eliminate the arbitrary use of revenues as the sole yardstick for measuring compliance.

A complaint by many banks involved in ETC development is that the ETCA has been interpreted and regulated by the Fed in a manner that puts the financial industry at a disadvantage. This in turn has dampened the vigor with which BHCs consummate ventures with nonfinancial institutions. The controversy revolves around application of the term *principally*, which was not defined in the statute. The Fed has interpreted it to mean at least 51 percent of revenues over a two-year period.

Finally, when a BHC–ETC must engage in a countertrade transaction in order to export U.S. products, and sells the goods received in trade to a third country, no credit is received for the export. Similarly, if the ETC engages in a trading transaction not involving U.S. export goods, the resulting revenues are offset against its export credits. In these two instances, the ETC is restricted in its ability to build trade relationships with foreign purchasers. This in turn discourages the development of a global trading mentality, which, in the longer term, would benefit U.S. export efforts.

Anomalies such as those cited above tend to slow the essential flow of equity capital that is needed to foster the trading industry.

DOC-Certified ETCs A second group of emerging ETCs are those receiving specific antitrust protection under ETCA. This new group of trading entities is as diverse in products as it is in size. Exports vary from fish to high technology. A few of these companies have annual sales in excess of $100 million, but the majority have sales of $10 million or less. In predicting their future development, it may be advisable to compare them with the export management companies (EMCs) to which they are closely related.

EMCs have been with us for a long time. They serve as manufacturers' representatives, often through becoming the international division of the companies they represent. It is estimated that the majority of EMCs, which are now believed to number less than 1,000, are small businesses, often small family enterprises. About 75 percent of EMCs do less than $5 million in gross sales per year. Largely ignored until recently by the federal authorities promoting trade, these companies are generally undercapitalized. Few of the existing government trade-support programs are of significant value to them. Tax incentives are too expensive for most, and the data base for expansion into new markets is either unavailable or too costly to develop. As a result, their opportunity to grow has been severely restricted.

The ability of EMCs to initiate small-business export projects is limited by the costs of sourcing outside the local geographic region. The larger EMCs dealing with manufactured products (there are possibly twenty to thirty with sales of $40 million and more) are very selective in extending their services to small businesses. From their perspective, it is expensive to bring these businesses into the international marketplace, and it requires a great deal of effort to identify, contact, and sell them on the merits of exporting. The new ETCs will face similar problems as the initial groupings seek to expand their marketing activities.

The impediments to small-business entry into the export market include (1) limited financial resources, (2) shortage of knowledgeable and available manpower, (3) uncertainties regarding the marketing of products internationally, (4) recognition of the emerging importance and complexity of countertrade, and (5) concern over the maintenance of domestic markets.

Federal funds for stimulating small-business exports have generally been allocated to states and other local governments, universities, trade associations, and a small number of private for-profit institutions. These efforts to assist individual small businesses to export on their own have met with marginal success, according to the General Accounting Office and a recent DOC report on this subject. The hoped-for marriage between trading companies and small businesses has not occurred.

Both ETCs and EMCs must now look through the spectrum of businesses to find medium-sized institutions that can provide the products, continuity of operation, and capital resources to sustain a sometimes long-term effort to develop overseas markets. Cost sharing on selected aspects of the trading process is common and may require considerable investment by the small producer who wishes to be supported.

What Is Needed

As noted above, a national strategy and program of activity to support small-business exporting, through the utilization of trade intermediaries, is urgently needed. The ETCA can be considered as an initial step in this process. However, without the development of a strong follow-up effort by government to support the initial legislation, little can be expected from ETCs in the near future.

The national program of support to trading intermediaries and small business is composed of many differing and often overlapping efforts. In the public sector, the departments of Commerce, Agriculture, State, Energy, and Education are funded in part to support export efforts. The Small Business Administration, Agency for International Development, Office of the U.S. Trade Representative, Export–Import Bank, and Overseas Private Investment Corporation, among others, receive annual appropriations to support the export drive. In short, contrary to popular opinion, there is no lack of funding directed toward the need to increase exports.

What is lacking is a cohesive program of activity to ensure that the hundreds of millions of dollars currently appropriated are more efficiently allocated. To this end, an interagency group, with leadership from the private sector, should be permanently established. The objective of this organization would be to further the development of trading institutions engaged in the promotion of small-business exporting. The relatively few funds needed—estimated at less than $10 million—could be transferred from the agencies noted above. A special appropriation to fund this activity would appear to be unnecessary.

A major role for the proposed institution would be the collection and dissemination of export-related data to ETCs and small businesses. The amount of information available in government files on export matters is staggering. However, this data is seldom extracted and organized into a form useful to the small business community. Sectoral analysis specifically oriented toward this segment of the trading community is needed. The institution could serve as the hub for data on sourcing and marketing, financing, export services, insurance, licensing, and regulatory matters. Gaps in the programmatic and informational systems of government agencies need to be identified, and corrective measures recommended. Finally, and of great importance, the institution could act as a catalyst to bring together small businesses with exportable products and trading institutions willing to take these goods to market.

Revitalizing the "Yankee Trader"

Correcting the U.S. trade imbalance requires the development of a strong commitment to trading companies and the small-business community. The ETCA requires amendment to encourage the financial community to invest further in trading institutions. Government needs a strategy to encourage and reward participation in the export drive. "Japan-bashing" and protectionism may offer short-term relief, but these palliatives only serve to further deter the necessary corrective action.

The establishment of a modestly funded, privately managed interagency institution to promote ETC and small-business trade is needed now. The necessity for plumbing the depths of a multitude of government departments and agencies to obtain information and other export support has placed unnecessary obstacles in the path of would-be trading institutions. Cohesive delivery of government services can be a small but essential step in the effort to revitalize the "Yankee Trader."

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NEWS OF THE COUNCIL

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SENATOR JOHN HEINZ (R-PA)

CETC TESTIMONY ON EXPORT TRADING COMPANIES

● Mr. HEINZ. Mr. President, Ron Wakeford, executive director of the Council for Export Trading Companies, is the author of some excellent testimony recently on the role of States in development of export trading companies.

Prepared for the Oversight and Investigations Subcommittee of the House Energy and Commerce Committees, Mr. Wakeford's testimony provides a thorough analysis of roles State and local governments might play in stimulating formation of ETCs.

The authors of the Export Trading Company Act of 1982, including myself, envisioned State and local governments stimulating ETC formation and in some cases participating in their formation. Some of this activity has already begun.

Later this year the International Finance Subcommittee of the Banking Committee, which I chair, will hold oversight hearings on the Export Trading Company Act and the way in which it has been utilized since its enactment in 1982. At that time I anticipate that Mr. Wakeford and other expert witnesses will appear.

Mr. President, I ask that Mr. Wakeford's statement be printed at this point in the RECORD.

The statement follows:

INTRODUCTION

THE ROLE OF STATES IN ETC DEVELOPMENT

(By Ronald C. Wakeford)

The purpose of this report is to address the question of: "What is an appropriate role for states and local governments to assume in the development of export trading companies (ETCs)?" Emphasis in this discussion is placed on improving the participation of small business in the exporting process through the development of public-private ETCs. In order to develop the key points of an argument suggesting that states can, and should play a major role in this area, I will comment on a number of related topics that identify the need for local government action. The topics are: Congressional and Administration recognition of the key role of states; obstacles, problems, and other impediments to small business exporting on their own; the marginal results obtained from past efforts to stimulate small business export; the present dearth of private sector intermediaries to support small business; the perceived role and actual programs of states; and a review of full-service ETCs and the role of states.

First, and for the record, let us look at the language used by Congress in considering the benefits to be derived by public sector participation in the development of ETCs. (See Fig. 1.) The underscoring has been added in the figure. The final statement in this illustration uses the terms organize, own, participate in or support ETCs. There seemed to be little doubt about the views of Congress on this subject.

To cap these words and lend support to Congressional statements, an administration spokesman noted with enthusiasm, shortly after passage of the Act, that some state legislatures were already working on: The development of state government affiliated ETCs; the creation of ETCs using partial state funding (public-private ETCs); and the establishment of export-import banks, guarantee loans for pre-export activities, and the sale of bonds for trade promotion activities.

It must be remembered that these statements, regarding the states and their role in the development and support of ETC development, were approved unanimously by both House and Senate. The Administration provided considerable support to Congress by emphasizing the need for ETC development in all sectors of the national economy. Political partisanship was not an issue, and neither was the question of local government interference in the private sector.

This latter point requires expansion to better understand the evolution of the ETC Act, especially as it concerned the status of small- and medium-sized businesses and the perceived need for trading companies of all kinds—private, public, and hybrid—to evolve.

IMPEDIMENTS TO SMALL BUSINESS EXPORTING

The Council for Export Trading Companies recently participated in a study for SBA to explore ways and means to develop an improved small business export expansion program. This effort paralleled, in part, the analyses undertaken by Congress in the development of the ETC Act and other small business export promotion programs. One aspect of this work involved a survey of small businesses, small business associations, and other public and private institutions to gather data on their attitudes towards exporting. The overwhelming response to the survey was that small business needed umbrella organizations or trade intermediaries to provide hands-on support to move their goods from loading dock to overseas buyers. In effect, small businesses were saying that they need to sell goods for export in the same manner as that of selling to a domestic wholesaler. Product modification and discounting to suit overseas market requirements presented no problem, but the perceived high risks and resource needs dissuaded them from exporting as a sole participant.

The impediments to solo entry included: (1) limited financial resources; (2) shortage of both knowledgeable and available manpower; (3) uncertainties regarding the marketing of products internationally; (4) recognition of the emerging importance and complexity of countertrade; and (5) concern over the maintenance of domestic markets. Let's pause for a moment to define business size which can be grouped, as shown in FIG. 2., into three categories. These categories include the Fortune 1000 industrials, a middle group with an employee base of over 500, and small business which is usually categorized as institutions with less than 500 employees. As noted in the figure, large- and medium-sized businesses are well served by their own international divisions or through trade intermediaries. However, small business is not generally served through the private sector for very good reasons.

PRIVATE SECTOR SUPPORT

As noted in the figure, there are two main institutions that could fulfill the comprehensive trade needs of small business, these are: export management companies (EMCs—often referred to as Title 1 ETCs); and the evolving ETCs. Let's look first at the EMCs. These have been with us for a long time and serve as manufacturers' representatives, often through the medium of becoming the international division of the companies they represent. It is estimated that the overwhelming majority of EMCs, which are estimated to number something less than 1000, are small businesses themselves, and that about 90 percent of EMCs do less than $3 million in gross sales per year. To develop and maintain profitability, EMCs must look upward through the spectrum of businesses to find those medium-sized institutions that can provide the products, continuity of operation, and capital resources to sustain a sometimes long-term effort to develop overseas markets. Cost-sharing on selected aspects of the trading process is common and may require a considerable investment by the small producer who wishes to be supported.

Similarly, the larger EMCs dealing with manufactured products, of which there are possibly 20-30 with sales of $40 million and greater, are very selective in the extension of services to small businesses. From their perspective, it is expensive to bring them into the international marketplace, and requires a great deal of effort to identify, contact, and sell them on the merits of exporting. The emerging Bank Holding Company ETCs are similarly restricted and are also reluctant to take on an unaffiliated small business that is new to exporting. This family of trading intermediaries, including EMCs of all sizes and BHC-ETCs, in the tough trading environment currently facing U.S. trade intermediaries, will not as a general rule: contract with or otherwise market the products of new-to-export small companies; and will consider engaging with small businesses having patented products, or otherwise proprietary item, or is considered a prominent manufacturer in the production of a line of goods.

In the latter instance, relatively few small business manufacturers can expect to obtain private sector EMC-ETC coverage without some form of support from the public sector.

A final category of a private sector trading intermediary is the Title 3 ETC, or those that are certified by the Department of Commerce. These institutions are comprised largely of small businesses that have joined together with other companies, often marketing similar products, to penetrate overseas markets. These institutions are growing in number and offer an exciting opportunity for export growth. But the thousands, if not tens of thousands, of small businesses with export potential still lack, at this time, practical umbrella organizations. Thus, the private sector ETCs offer only limited oportunities to the small business manufacturer.

THE FEDERAL PROGRAMS TO STIMULATE SOLO EFFORTS

The federal funds allocated to the task of stimulating small business exports have generally been allocated to states and other local government, universities, trade associations, and a small number of private for-profit institutions. These efforts to assist individual small businesses to export on their own has only met with marginal success. Gao and other Congressional information, and more recently a Department of Commerce report on this subject, all attest to the failure or marginal utility of these programs to make significant progress.

In one instance, the DOC funded sixteen organizations in October 1982, including thirteen states and local government entities, and three other institutions. The maximum grant available was $150,000 and a total of $4 million was expended (including the cost share of 50 percent). The objectives of the program was "encouraging the development and implementation of a small business international marketing program". In commenting on the performance of the grant recipients, the report noted that the total amount of "new to market/new to export sales generated" was only $4.3 million. The DOC report stated flatly that the $4.3 million figure was probably inflated and that "grants are not an effective method for encouraging development of continuing self-sustaining small business international marketing programs".

With the growing emphasis on "federalism", it is unlikely that we will see an expansion of funded federal programs to further stimulate small business export expansion. Further reliance on the states to service this need will tend to be the theme struck with considerable emphasis during the coming years.

STATE PROGRAMS

With the private sector and federal efforts tending to strike out in the small business export expansion program, let's look at the role of the states.

Of serious concern to all states is the maintenance or further development of their industrial or manufacturing base. To this end, most states spend sizeable amounts on encouraging industry to relocate to their territory. Of parallel importance, in many instances, is the delivery of a strong export program to provide further incentives to the transfer facilities. Similarly, the encouragement of foreign enterprises to relocate occupies a significant proportion of time spent by state employees located overseas. Their success in the future may well depend upon a parallel and an increasingly aggressive program to move the goods produced into the world trade stream.

Each state has developed its own particular form of small business support to exporting and, in a few instances, to the establishment of ETCs. This has been based on its own economic development objectives and exporting capability. The types of assistance provided can be discusses under three major headings, these are: (1) information dissemination; (2) organizational and service support; and (3) direct participation (See Fig. 3.)

The figure shows a spectrum of activity ranging from the passive informational approach to that of developing a fully-owned and operated state ETC. As the trade deficit worsens, most states are becoming more aggressive in their roles and are moving rapidly towards the "hands-on" support effort characterized by the term Direct Participation.

FULL-SERVICE ETC'S

The remaining question is how *far* have the states already progressed toward the provision of ETC services and what further steps would be necessary to bridge remaining gaps. If the activities of a full-service ETC are divided into three components, they would consist of: (1) market analysis, development and sales; (2) trade flow management; and (3) trade financing. Fig. 4 provides information on the activities associated with each of these headings.

In reviewing the tasks identified in the figure, it becomes apparent that many states, especially those with port authorities accomplish many of the functions listed and require only the establishment of cohesiveness within existing state activities to establish public or public-private sector ETCs. Of the three major roles, trade flow management is well within the grasp of port authorities with a minor expansion of capability needed in some instances. Landlocked states have, in a number of instances, established working relationships with port authorities in other states to round out their trading capability. Regional efforts to further develop this practice and build multistate ETC capability, either by product area or international market focus, can enhance the probability of export success for all involved in the venture.

As noted previously, trade financing is underway in some 20 states and does not require further discussion. The most difficult aspect of the problem can be found under the heading: Market Analysis, Development and Sales.

Many of the activities illustrated in the figure are already being accomplished by states, however, countertrade assessment and related action programs are still to be grappled with in most public sector organizations. Similarly, market entry strategy and business planning by product or commodity area tends to be lacking. Finally, direct sales to foreign customers has not been a traditional role for the states, although states and port authorities with overseas offices have been "selling services" for a lengthy period. These gaps, in the overall spectrum of activities that a full-service ETC would fill, are not difficult barriers to surmount. To the contrary, trained manpower already exists, and on-the-job training can be undertaken to fill gaps in capability.

STRATEGY FOR THE FUTURE

In evaluating the future role of states in promoting small business exports and the development of ETCs, there appears to be three principal options, these are: To provide the major stimulus for the evolution of trading companies within the state; a hybrid approach aimed at the development of a public-private sector ETC using existing capabilities that are available in both areas of the economy; the establishment of state-owned, managed, and operated ETCs based upon the expansion or unification of public capability in the export field.

Although both the first and third options have considerable merit, it is the second option that appears to be most advantageous for small business export development in the near term. Accordingly, the following comments have been restricted to a discussion of the hybrid approach.

A PUBLIC-PRIVATE ETC

To summarize the potential role of states in expanding ETCs in support of small business, an illustration has been prepared to show how one such entity can be constructed from both private and public sector resources. (See fig. 5)

The figure shows a mixture of public-private relationships that are practical and can be developed without injury to either sector of the economy. Little needs to be said about the relationships that already exist in the Trade Flow Mangement area where port authorities routinely interact with freight forwarders, warehousers, and transportation firms. Similarly, in the Financing area, public and private sector combinations are already at work to simplify the funding of both purchaser and buyer in the export field. Some activities associated with Market Analysis, Development, and Sales, however, will need support from the private sector to round out the achievement of ETC capabilities.

As shown in the figure, the state ETC can draw upon existing federal information and other services and some key personnel from the private sector. This public-private entity can also be the catalyst for the evolution of private sector ETCs, but state programs are needed in the near term to bridge the burgeoning trade gap.

CONCLUSIONS

In conclusion, it can be shown that: The states have a clear mandate and singular responsibility to promote small business exports by organizing, owning, or participating in the development of an ETC or ETCs; federal program support and private intermediaries have not or cannot bring small businesses to market in sufficient number to substantially improve the U.S. trading posture; many states are already involved in aggressive and comprehensive programs that simulate ETC activities; only a modest additional effort may be required, in many instances, to adapt present programs and develop a full-service ETC; and an opportunity is provided to combine public and private capabilities without impinging on the role of either segment of the economy.

Figure 1.—Public Participation in the ETC Development Process

The ETC Act of 1982—title 1, sec. 102(A)(8): Those activities of State and local governmental authorities which initiate, facilitate, or expand exports can be an important source of expansion of U.S. exports (and) for experimentation in the development of innovative export programs.

Conference report on S. 734: State and local government entities, including port authorities, to continue their efforts including their ability to organize, own, participate in, or support ETC.

Figure 2.—Business Profiles

Mode of export operations: Large: Multinationals, International division; Fortune 1000 companies, some fully-owned ETCs; special market ETCs.

Needs: Small: Well serviced. Minimal reliance on external ETCs.

Mode of export operations: Medium: More than 500 employees, international division; less than $125 million, exports through ETCs.

Needs: Modest: Able to operate independently or through existing trade intermediaries.

Mode of export operations: Small: Less than 500 employees, some "do it yourself" activity; high-tech, patentable products, ETC attention; majority do not export.

Needs: Extensive: Hands-on and comprehensive support needed, gap in private intermediary coverage.

Figure 3.—State Export Activity Grouping

Information dissemination:

Advisory services on Federal programs; newsletters on trade; sponsorship or cosponsorship of export seminars; directories of export services; export guides.

Organizational and services support:

Catalogs and promotional material; outreach and councilling; statewide survey of export potential; State-developed trade leads; matchmaking and distributor identification.

Direct participation:

Trade missions and shows; overseas promotional offices; market analysis by industry and company; trade financing programs; public sector ETC development.

Figure 4.—Full-Service ETC's and State Opportunities

Market analysis, development and sales:

Sourcing—analysis of small business export base; market research by international region or country, and by product area; countertrade assessment; market entry strategy and business plan; identification and selection of distributors; advertising, promotion, and public relations; negotiations and sales.

Trade flow management:

Inland transportation; packaging—labeling; goods-in-transit insurance and freight; customs clearance; documentation; shipping; warehousing; overseas inland transportation; follow-up services.

Trade financing:

Pre-export financing for small business; goods-in-transit financing (short, medium-term); risk lay-off insurance and guarantees; buyer financing (short, medium and long-term).

Figure 5.—A Public-Private Hybrid ETC

AN ORGANIZATIONAL OPTION FOR A FULL SERVICE PUBLIC-PRIVATE SECTOR ETC FOR SMALL BUSINESS

Financing:

Public sector: Appropriations; bonds; loan guarantees.

Private sector: State bank loans; insurance companies; other private.

Trade flow management:

Public sector: Port authorities; industrial development corporations.

Private sector: Local transport; warehousing.

Market analysis development, and sales:

Public sector: Sourcing, strategy and business planning; overseas offices.

Private sector: International business and consulting firms.

With support from: Federal information services; State export programs and overseas offices; small business and private sector supporting institutions.●

Mr. **Barnard**. Our next panel represents the banks who have had experiences in the export trading company area: Mr. James Brannen, senior vice president of the First National Bank of Chicago, and Mr. R. Michael Rice, president of Chase Trade, Inc. If you gentlemen would please take your places at the table.

I always want to thank our panelists who have been here from the very beginning of the hearing, because you have been sitting here for some time listening to all this testimony. I'm sure that that in itself is somewhat fatiguing. But we're delighted to have you here this morning and appreciate very much the benefit of your experience and the testimony that you have offered our committee.

Mr. Brannen and Mr. Rice, normally we include your entire testimony, without objection, in the record and would hope that you might be able to summarize. So we will hear from you first, Mr. Brannen.

STATEMENT OF JAMES S. BRANNEN, SENIOR VICE PRESIDENT, FIRST NATIONAL BANK OF CHICAGO

Mr. **Brannen**. I would be happy to do so.

Mr. Chairman and members of the subcommittee, my name is James Brannen. I'm a senior vice president, First National Bank of Chicago, the principal subsidiary of First Chicago Corp., a bank holding company. I was also president of Sears-First Chicago Trading Co., an export trading company, from its inception in 1983 until July 1985.

First Chicago participates in export trading company activities through two entities. First Chicago Trading Co. is a wholly owned subsidiary of First Chicago Corp., and the second ETC is a 50-50 partnership formed by First Chicago Trading and Sears World Trade, Inc. It is our intent to use First Chicago Trading for structuring trade finance transactions and business which originates with our customers and does not fit the Sears World Trade strategy. On the other hand, we expect the bulk of our trade activities to be done in the partnership with Sears, and that has been our experience to date. First Chicago entered into this arrangement with Sears World Trade for three principal reasons.

First, it was the corporation's desire to establish a significant level of activity in the export trading business, but to do so in a way that would not require the bank to invest all the necessary capital.

Second, First Chicago needed access to a substantial worldwide distribution network and believed that such a network could most readily be developed by working in cooperation with a partner who had experience in buying and selling goods in global markets.

Third, we recognized that the prevailing culture at First Chicago, while appropriate to banking, was not ideal for the trading business.

Our partnership with Sears World Trade commenced in December 1983, and we continue to believe it is the appropriate vehicle for most transactions we will undertake in this business. Sears-First Chicago Trading Co. earned a modest profit in 1985 and is expected to be profitable in 1986 as well.

Examples of the types of business we have done since formation 2 years ago are as follows:

We have performed two consulting assignments for small Midwestern companies with respect to the sale of products and equipment in China.

We located a Far East manufacturer of electronic sound equipment, exchanged specifications between buyer and seller, purchased the component, and shipped it to a Midwestern manufacturer of hospital communications equipment.

We located a low-cost source for an electronic component for a Midwest toy manufacturer. We provided cargo management and import financing in addition to the sourcing effort.

We provided consulting assistance and prepared a proposal for a large Midwestern company relative to the countertrade aspects of a telecommunications project they were bidding on in the Middle East.

We have located United States buyers for Uruguayan-produced lactic casein, a milk byproduct used in glues.

We have provided consulting assistance to a Mexican manufacturer of automobile parts who was considering entering the United States market.

We have provided import financing assistance, cargo management, and customs clearance services for a new U.S. company importing toys. This activity involved everything from chartering airplanes to assisting in making sure the customs classifications were accurate.

We provide United States companies with setup and management services in the Virgin Islands relative to foreign sales corporations. Currently we manage about 50 of these companies.

We worked with a United States company to export logs to China.

In all candor, Mr. Chairman, while we have been able to generate a number of diverse trading company transactions and relationships, the earnings and the level of activity attained to date have fallen short of our original expectations. As a consequence, we have reorganized the staff and put the marketing and execution thrust back into the two partner organizations. We now operate with a very low overhead and rely on each partner's staff to generate our business.

But the problems we have encountered to date in doing export-related projects are not entirely internal in origin. They are external in nature as well. I would like to take note of four external difficulties we have had to deal with.

First, and perhaps most obvious, was the high value of the dollar. The adverse impact of the strong dollar on American exports is well known to this committee, and we need not dwell on that today.

Second, many of the countries where we would normally look for customers are faced with high external debt and are reacting to pressures from international agencies and institutions by encouraging their own exports and discouraging imports.

The third external problem we have faced is related to the fact that the American companies continue to prefer to expand their U.S. sales instead of seeking overseas opportunities where product and packaging adjustments might be required. The U.S. marketplace is, of course, a vast and attractive one. Understandably, therefore, when it proves more difficult to enter a foreign market than one in the United States, American companies are inclined to prefer domestic expansion over pursuit of foreign opportunities.

In such a setting, Mr. Chairman, it is very difficult for independent trading companies to create a desire among U.S. companies to expand their horizons. It is no coincidence that most successful trading companies have developed where the domestic market opportunities were limited.

The fourth external challenge I want to mention is the fact that newly formed independent trading companies face very stiff competition. It is appropriate to note that new export trading companies must contend with competition from European, Japanese, and Asian trading companies that have been in business for a long time. There are also more than 2,400 small export management companies in the United States that have developed specialized niches for themselves over the past 50 years. In addition, most major U.S. companies have years of experience and long histories of contacts with markets worldwide.

In the case of Sears-First Chicago Trading Co., operations began with a very narrow base of experience. On the bank side, we had officers around the world and good contacts in foreign countries, but our people were financial experts, not traders. On the Sears side, they had great experience buying and moving goods around the world and had offices around the globe, but understandably Sears did not have broad experience in developing overseas distribution capability beyond their own retail stores' operations.

For 2 years now, Sears-First Chicago Trading Co. has been forging an approach which will capitalize on the strengths of the two parent companies. That approach holds out a very real prospect of building over time a significant export-import trading business. Nevertheless, this cannot be achieved overnight.

What is more, Mr. Chairman, trading, the highly entrepreneurial business of matching buyers and sellers, identifying attractive markets, and finding low-cost or high-quality producers, is a business of surprisingly thin profit margins. A successful trading company thrives on a good information base which includes knowledge of products and markets, responsiveness, and timeliness. It cannot afford to support elaborate systems and costly overheads built to respond to Government reporting and regulatory requirements.

It is also a business that will be of increasing importance to our Nation as the need to export continues to be acute, and it cannot grow and prosper if saddled with burdensome regulatory controls. Accordingly, trading companies merit and can use the encouragement that is implicit and explicit in a supportive regulatory environment.

In this context, I'd like to comment on some major regulatory issues. As a preface, I'd say that the Federal Reserve Board has moved very cautiously in its regulation of ETC's, in part due to its lack of experience in regulating these kinds of entities, in part as a result of ambiguities in the legislation, and in part due to the inexperience of the banks involved in operating ETC's. Let me add that

I believe the banks, too, have moved cautiously, and it has been appropriate that they do so.

We don't believe that the Federal Reserve Board has been obstructive. Still in all, we are of the opinion that the Board may be moving a bit too cautiously. The first regulatory issue I'd like to address is that of the so-called 50-percent rule. This rule requires that more than 50 percent of our income must come from exports. Specifically, the 50-percent export revenue rule is unduly restrictive, given the adverse balance of trade that is currently being experienced by the United States. Sears-First Chicago Trading Co. was able to meet the test in the first 2 years largely because of revenues from the foreign sales corporation startups. Currently, however, we are seeing fewer export opportunities and many more opportunities to help U.S. companies lower their costs of production through offshore sourcing of component parts.

Additionally, it seems to us illogical to include revenue from third-country transactions in the revenue base for purposes of this calculation. These revenues have no impact on the U.S. balance of trade.

In addition, given the nature of current trade conditions and the need for ETC's to build their distribution capability in global markets and, at the same time, generate some revenues in order to cover high startup costs, it is unrealistic that these regulatory revenue targets be met within a 2-year timeframe.

Mr. Chairman, we at First Chicago respectfully suggest that the regulatory time horizon be extended from 2 to 10 years. In this context, it may be appropriate to take note of the fact that in many cases our activities related to imports actually help create jobs in the United States that otherwise would not exist.

If I may, let me cite as an example a toy product that we are helping a new U.S. company import. The cost of the toy to the American company is less than $24 landed in the United States, and the toy simply cannot be manufactured in this country for that cost. The U.S. company then adds marketing, advertising, packaging, and a number of other services before the toy is transported to the retailer. Costs incurred in the United States raise the price of the toy to $70.

Thus, out of a volume that exceeded $100 million this year, only a third represents amounts paid overseas, and two-thirds of the sales dollars stayed in the United States—paying salaries and wages and supporting more than——

Mr. **Barnard**. Is that that bear for children?

Mr. **Brannen**. Yes; it is.

Mr. **Barnard**. I bought one.

Mr. **Brannen**. You did? Supporting more than 100 new jobs in addition to adding work for other people in the distribution chain.

Finally, with respect to the revenue test, we feel that the exporter services produced by an ETC or an affiliate should be counted as export-related income to the extent that these revenues are related to U.S. exports of goods or services.

The second regulatory issue I would like to address involves asset-to-capital ratios. It is our current understanding that the Board has an international guideline that permits an export trading company to have assets 10 times its capital, but beyond that the Board has to give its approval. This process creates problems for us in being able to give timely responses to customers when leverage ratios exceed 10 to 1. It is our view that this ratio should be raised to 25 to 1 inasmuch as this higher ratio is more consistent with the requirements imposed on our competitors throughout the world. Furthermore, this higher ratio is consistent with the Board's overall guidelines for capital adequacy applied to bank holding companies.

Mr. Chairman, we believe the best way to accomplish such a change legislatively would be to have a provision that states the Board may not establish by regulation a capital adequacy limit of less than 25 to 1. They have ample opportunity during the examination process to ensure that ETC's adopt appropriate policies and procedures concerning taking title to goods and other issues which affect leverage.

The amount of leverage alone is not really the central issue. Rather, it is the quality of the assets and the amount of risk that the value of the assets may deteriorate. It is both possible and appropriate to incur enormous leverage in a transaction when that transaction involves virtually no risk. Let me cite an example.

A trading company might be asked to purchase from an American company inventory of a commodity nature for which there is a sales contract for delivery of the inventory at a future date. Both the purchase and sales price plus the "cost of carry" may be fixed. If the buyer has an unquestioned ability to pay, then the risk in the transaction is very small.

We encountered such a situation with respect to the export of logs from the United States. We are currently facing similar circumstances in a transaction involving the importation of oil into the United States.

A third regulatory issue to which I'd like to invite your attention is that of the regulatory requirements of section 23A of the Federal Reserve Act. To get to the heart of the matter, Mr. Chairman, we support the elimination of those collateral requirements.

We believe the collateral requirements of section 23A may have resulted from an oversight when the revisions of this section were made by Congress in 1983, and we believe that they are unduly burdensome. We further believe that the existing requirements that limit credit to no more than 10 percent of the affiliated bank's capital and surplus and which require that credit be granted on nonpreferential terms are adequate.

The final regulatory issue that I would like to address today is that of inventory policies. Specifically, we feel that ETC's should be permitted to establish their own inventory policies and not be subjected to an arbitrary number such as $2 million beyond which special approvals are required.

The mere holding of inventory need not entail risk. Moreover, transaction opportunities frequently arise quickly. In such circumstances, we do not have the luxury of time it takes to get regulatory approval for all the exceptions. In our view, the Board should examine inventory policies adopted by each ETC. If they judge those policies to be unsound or unduly speculative, they should then initiate corrective action.

Mr. Chairman, your invitation to testify today solicited comments on certain statements by the Board. Specifically, they have said that they will grant waivers and are therefore flexible in responding to bank ETC difficulties with regulatory requirements. Furthermore, the Board has stated that its regulations are necessary to maintain an adequate barrier between commerce and banking, to carry out congressional intent with respect to exports, and to assure the safety and soundness of our Nation's banking system.

It is our view that it is the Board's intention to be responsive and flexible. However, experience has shown that approvals require both time and extensive justifications that, in the light of the vagueness of sections of the regulations, make it difficult for banks to obtain approval in a timely manner. The law establishes an adequate barrier between commerce and banking by limiting credit extensions to the ETC by the affiliated bank. With this barrier, the Board essentially prevents the bank from placing an inordinate amount of credit or the bank's capital at risk in the ETC.

In closing, I'd like to respectfully suggest two additional changes that would streamline the ETC regulations. First, I would recommend that the Board adopt a general consent provision similar to that contained in regulation K for foreign subsidiaries. This would permit fairly modest investments in ETC's without their specific approval. Regulation K now allows foreign investments up to the lesser of $15 million or 5 percent of the investor's capital and surplus under general consent. This change could eliminate some of the delays that prevent the making of timely investments.

My second suggestion is that ETC's be given general powers to engage, without seeking Board approval, in any activities that are expressly permitted under the ETC Act. Under current regulations, specific approval is needed for title taking, product research and design, and product modification.

Particularly in the area of title taking, Board approval may lead to significant delays in taking advantage of business opportunities.

Mr. Chairman, we continue to be enthusiastic about the role of our ETC's and that role which they can play in enabling us to finance trade and encourage U.S. companies, particularly small- and medium-sized concerns, to recognize that their participation in global markets is both feasible and economical.

Thank you for this opportunity to appear before you today. If you have questions, I'd be glad to respond.

[The prepared statement of Mr. Brannen follows:]

Statement of James S. Brannen

President of Sears-First Chicago Trading Company

and

Senior Vice President, The First National Bank of Chicago

before the

Commerce, Consumer, and Monetary Affairs Subcommittee

of the

Committee on Government Operations

March 4, 1986

Washington, D.C.

Mr. Chairman, and members of the Subcommittee, my name is James S. Brannen. I am a Senior Vice President at The First National Bank of Chicago, the principal subsidiary of First Chicago Corporation, a bank holding company. I was also President of Sears-First Chicago Trading Company from its inception in December, 1983 until July, 1985.

First Chicago participates in export trading company activities through two entities. First Chicago Trading Company is wholly-owned by First Chicago Corporation and the second ETC is a 50/50 partnership formed by First Chicago Trading Company and Sears World Trade, Inc. (See Exhibit A). It is our intent to use First Chicago Trading Company for structuring trade finance transactions and business which originates with our customers and does not fit the Sears World Trade strategy. On the other hand we expect the bulk of our trade activities to be done in the partnership and that has been our experience to date. First Chicago entered into this arrangement with Sears World Trade for three principal reasons:

First, it was the Corporation's desire to establish a significant level of activity in the export trading business, but to do so in a way that would not require the bank to invest all the necessary capital.

Second, First Chicago needed access to a substantial worldwide distribution network and believed that such a network could most readily be developed by working in cooperation with a partner who had experience in buying and selling goods in global markets.

Third, we recognized that the prevailing culture at First Chicago, while appropriate to banking, was not ideal for the trading business. Banks are more comfortable dealing with credit risk, financial assets and spreads than with performance risk, product values and gross margins. The latter are the tools of the export trader.

Our partnership with Sears World Trade commenced business in December, 1983, and we continue to believe it is the appropriate vehicle for most transactions we will undertake in this business. Sears-First Chicago Trading Company earned a modest profit in 1985 and is expected to be profitable in 1986 as well.

Examples of the types of business we have done since formation two years ago are as follows:

1. We provided consulting assistance to a Midwest manufacturer of large, mobile dynamometers who were negotiating a sale to China. Our assistance included helping our customer understand Chinese methods of doing businss and making sure price arrangements would permit them to make a profit on the sale.
2. A second project related to China involved consulting help on shipping arrangements for a large piece of foundry equipment and providing a guarantee of payment upon proper presentation of documents.
3. We located a Far Eastern manufacturer of electronic sound equipment, exchanged specifications between

buyer and seller, purchased the product and shipped it to a Midwest manufacturer of hospital communications equipment.

4. We located a low cost source for an electronic component for a small Midwest toy manufacturer. We provided cargo management and import financing in addition to the sourcing effort.
5. We provided consulting assistance and prepared a proposal for a large Midwestern company relative to the countertrade aspects of a telecommunications project on which they were bidding in the Middle East.
6. We have located U.S. buyers for Uruguayan produced lactic casein, a milk by-product used in glues and other products. We purchased the product in Uruguay, shipped it to the U.S. and arranged for delivery to the U.S. company.
7. We provided consulting assistance to a Mexican manufacturer of automobile parts who was considering entering the U.S. market. The assignment included determining if product quality met U.S. standards, designing and evaluating packaging, identifying channels of distribution and making recommendations for a marketing strategy.
8. We provided import financing assistance, cargo management and customs clearance services for a new U.S. company importing toys. This activity involved everything from chartering airplanes to assisting in making sure the customs classifications were accurate.

9. We provide U.S. companies with set-up and management services in the Virgin Islands relative to foreign sales corporations. Currently we manage about 50 such companies.
10. We worked with a U.S. company to export logs to China. This activity was principally financing related. We purchased the logs on behalf of a timber sales company and held title to them until they were loaded on ships and accepted by the buyer.

In all candor, Mr. Chairman, while we have been able to generate a number of diverse trading company transactions and relationships, the earnings and the level of activity attained to date have fallen short of our original expectations. As a consequence, we have reorganized the staff and put the marketing and execution thrust back in the two partner organizations. We now operate with very low overhead and rely on each partners' staff to produce our business.

But the problems we have encountered to date in doing export-related projects are not entirely internal in origin. They are external in nature, as well. And I would like to take note of four external difficulties with which we have had to deal.

First, and perhaps most obvious, was the high value of the dollar. The adverse impact of the strong dollar on American exports is well known to this Committee and needs no further discussion here today.

Second, many of the countries where we would normally look for customers are faced with high external debt and are reacting to pressures from international agencies and institutions by encouraging exports and discouraging imports.

The third external problem we have faced is related to the fact that American companies continue to prefer to expand their U.S. sales instead of seeking overseas opportunities where product and packaging adjustments may be required. The U.S. marketplace is, of course, a vast and attractive one. Understandably, therefore, when it proves more difficult to enter a foreign market than one in the U.S., American companies are inclined to prefer domestic expansion over pursuit of foreign opportunities.

In such a setting, Mr. Chairman, it is very difficult for independent trading companies to create a desire among U.S. companies to expand their horizons. It is no coincidence that most successful trading companies have developed where the domestic market opportunities were limited.

The fourth external challenge I want to mention is the fact that newly formed independent trading companies face very stiff competition. It is appropriate to note that new export trading companies must contend with competition from European, Japanese, and Asian trading companies that have been in business for a long time. There are also more than 2,400 small export management companies in the U.S. that have developed specialized niches for themselves over the past 50 years. In addition, most major U.S. companies have years of experience and long histories of contacts with markets worldwide.

In the case of Sears-First Chicago Trading Company, operations began with a very narrow base of experience. On the bank side, we had offices around the world and good contacts in foreign countries. But our people were financial experts not traders. On the Sears side, they had great experience buying and moving goods around the world and had offices around the globe. But, understandably, Sears had not had broad experience in developing overseas distribution capability beyond their retail stores operations.

For two years, now, Sears-First Chicago Trading Company has been forging an approach that will capitalize on the strengths of the two parent companies. That approach holds out the very real prospect of building, over time, a significant export-import trading business. Nevertheless, this cannot be achieved overnight.

And what is more, Mr. Chairman, trading -- the highly entrepreneurial business of matching buyers with sellers, identifying attractive markets, and finding low-cost or high quality producers -- is a business of surprisingly thin profit margins. A successful trading company thrives on a good information base which includes knowledge of products and markets, responsiveness and timeliness. It cannot afford to support elaborate systems and costly overheads built to respond to government reporting and regulatory requirements.

It is also a business that will be of increasing importance to our nation as the need to export continues to be acute. And it cannot grow and prosper if saddled with burdensome regulatory controls. Accordingly, trading companies merit and can use the encouragement that is implicit and explicit in a supportive regulatory environment.

In this context, I would like to comment on some major regulatory issues. I will identify these issues, describe their actual or anticipated impacts on Sears-First Chicago Trading Company, and offer suggestions for appropriate regulatory changes.

As a preface, I would say that the Federal Reserve Board has moved very cautiously in its regulation of ETC's in part due to its lack of experience in regulating these kinds of entities, in part as a result of ambiguities in the legislation and in part due to the inexperience of the banks in operating ETC's. Let me add that I believe the banks too have moved cautiously and it has been appropriate that they do so.

We don't believe that the Federal Reserve Board has been obstructive. Still in all, we are of the opinion that the Board may be moving a bit too cautiously with regard to permitting bank holding companies to utilize their ETC's to take advantage of trading opportunities.

The first regulatory issue that I would like to address is that of the so-called "fifty percent rule." This rule requires that more than 50% of an ETC's income must come from exports. Specifically, the 50% export revenue rule is unduly restrictive, given the adverse balance of trade that is currently being experienced by the United States. For example, Sears-First Chicago Trading Company was able to meet the test in its first two years of existence largely because of revenues from the foreign sales corporation start-ups. Currently, however, we are seeing fewer export opportunities and many more opportunities to help U.S. companies lower their costs of production through offshore sourcing of component parts.

It seems to us illogical to include revenue from third country transactions in the revenue base for purposes of this calculation. These revenues have no impact on the U.S. balance of trade. Trading companies are participants in global markets, and it is short sighted and even unfair to penalize us for economic conditions around the world over which we have no control.

In addition, given the nature of current trade conditions and the need for ETCs to build their distribution capability in global markets and at the same time generate revenues in order to cover high start-up costs, it is unrealistic to require that these regulatory revenue targets be met within a two-year time frame.

Mr. Chairman, we at First Chicago respectfully suggest that the regulatory time horizon be extended from two to ten years.

In this context, it may be appropriate to take note of the fact that, in many cases, our activities related to imports actually help create jobs in the United States that otherwise would not exist. If I may, let me cite as an example a toy product that we are helping a new U.S. company import.

The cost of the toy to the American company is less than $24 landed in the U.S. And the toy simply could not be manufactured in this country for that cost. The U.S. company then adds marketing, advertising, packaging and a number of other services before the toy is transported to the retailer. Costs incurred in the United States raise the price of the toy to $70. Thus, out of a volume that exceeded $100 million this year, only a third represents amounts paid overseas and two thirds of the sales dollar stayed in the U.S., paying salaries and wages and supporting more than 100 new American jobs in addition to adding work for numerous other support people throughout the distribution chain.

Finally, with respect to the revenue test, we feel that the export of services produced by an ETC or an affiliate should be counted as export-related income to the extent that those revenues are related to U.S. exports of goods or services. While this provision has not had an impact on our operations to date, I can see where we might find it necessary to establish a warehousing venture in connection with a given U.S. export project. Such a step would be a legitimate export activity, and it could also afford us an important measure of protection and profitability in structuring a transaction.

The second regulatory issue I would like to address involves asset to capital ratios. It is our current understanding that the Federal Reserve Board has an internal guideline that permits an export trading company to have assets ten times its capital, but beyond that the Board has to give its approval. This process creates problems for us in being able to give timely responses to customers when leverage ratios exceed 10:1. It is our view that this ratio should be raised to 25-to-1, inasmuch as this higher ratio is more consistent with the requirements imposed on our competitors throughout the world. Furthermore, this higher ratio is consistent with the Board's overall guidelines for capital adequacy applied to bank holding companies.

Mr. Chairman, we believe that the best way to accomplish such a change legislatively would be to have a provision that states that the Board may not establish by regulation a capital adequacy limit of less than 25:1. They have ample opportunity during the examination process to insure that ETC's adopt appropriate policies and procedures concerning taking title to goods and other issues which affect leverage.

The amount of leverage alone is not really the central issue. Rather, it is the quality of the assets and the amount of risk that the value of the assets may deteriorate.. It is both possible and appropriate to incur enormous leverage in a transaction when that transaction involves virtually no risk. Let me cite an example.

A trading company might be asked to purchase from an American company inventory of a commodity nature for which there is a sales contract for delivery of the inventory at a future date. Both the purchase and sales price, plus the "cost of carry" may be fixed. If the buyer has an unquestionable ability to pay, then the risk in the transaction is very small.

We encountered such a situation with respect to the export of logs from the U.S. We are currently facing similar circumstances in a transaction involving the importation of oil to the U.S.

A third regulatory issue to which I would like to invite your attention today is that of the regulatory requirements of Section 23A of the Federal Reserve Act as they apply to ETCs.

To get to the heart of the matter Mr. Chairman, we support the elimination of those collateral requirements. We believe the collateral requirements of Section 23A may have resulted from an oversight when the revisions to this section were made by Congress in 1983, and we believe that they are unduly burdensome. We further believe that the existing requirements that limit credit to no more than 10% of the affiliated bank's capital and surplus, and which require that credit be granted on non-preferential terms, are adequate.

The final regulatory issue that I would like to address today is that of inventory policies.

Specifically, we feel that ETCs should be permitted to establish their own inventory policies and not be subjected to an arbitrary number, such as $2 million, beyond which special approvals are required. The mere holding of inventory need not entail risk. Moreover, transaction opportunities frequently arise quickly. In such circumstances, we do not have the luxury of the time it takes to get regulatory approval for all exceptions. In our view, the Board should examine inventory policies adopted by each ETC. If they judge those policies to be unsound or unduly speculative, it should then initiate corrective action.

Mr. Chairman, your invitation to testify at today's hearing solicited comments on certain statements by the Board. Specifically, they have said that it will grant waivers and is, therefore, flexible in responding to bank ETC difficulties with regulatory requirements. Furthermore, the Board has stated that its regulations are necessary to maintain an adequate barrier between commerce and banking, to carry out Congressional intent with respect to exports, and to assure the safety and soundness of our Nation's banking system.

It is our view that it is the Board's intention to be responsive and flexible. However, experience has shown that approvals require both time and extensive justifications that, in light of the vagueness of sections of the regulations, make it difficult for banks to obtain approval in a timely manner. The law establishes an adequate barrier between commerce and banking by limiting credit extensions to the ETC by the affiliated bank. With this barrier, the Board essentially prevents the bank from placing an inordinate amount of credit, or the bank's capital, at the risk in the ETC.

In closing, Mr. Chairman, I would like to respectfully suggest two additional changes that would streamline the ETC regulations in a constructive fashion.

First, I would recommend that the Board adopt a general consent provision similar to that contained in Regulation K for foreign subsidiaries. This would permit fairly modest investments in ETCs without their approval. Regulation K now allows foreign investments up to the lesser of $15 million or 10% of the investor's capital and surplus under general consent. This change could eliminate some of the delays that prevent the making of timely investments.

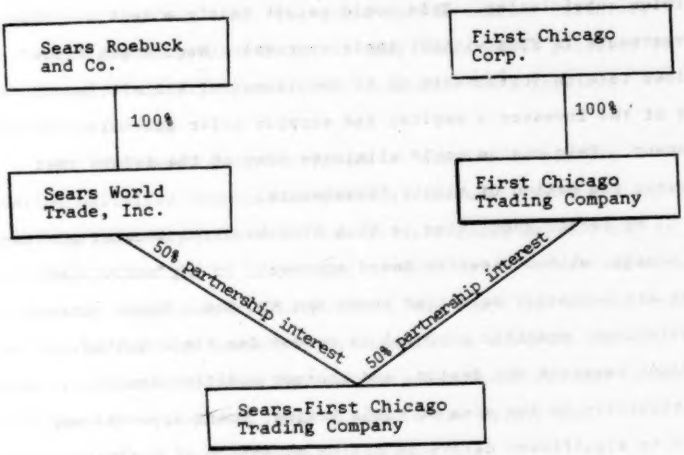
My second suggestion is that ETCs be given general powers to engage, without seeking Board approval, in any activities that are expressly permitted under the ETC Act. Under current regulations, specific approval is needed for title taking, product research and design, and product modification. Particularly in the area of title taking, Board approval may lead to significant delays in taking advantage of business opportunities.

Mr. Chairman, we continue to be enthusiastic about the role our ETCs can play in enabling us to finance trade and encourage U.S. companies, particularly the small and medium sized concerns, to recognize that their participation in global markets is both feasible and economical.

Thank you for this opportunity to appear before your Subcommittee today. If you have any questions, I will be pleased to respond to them.

EXHIBIT A

OWNERSHIP STRUCTURE


Sears Roebuck and Co.
First Chicago Corp.
100%
100%
Sears World Trade, Inc.
First Chicago Trading Company
50% partnership interest
50% partnership interest
Sears-First Chicago Trading Company

Mr. Barnard. Thank you, Mr. Brannen.

We will now hear from Mr. Rice.

STATEMENT OF R. MICHAEL RICE, PRESIDENT, CHASE TRADE, INC.

Mr. Rice. Thank you, Mr. Chairman and members of the committee.

My name is Michael Rice. I am president of Chase Trade, Inc., which is Chase Manhattan Corp.'s export trading company. It's a great pleasure to be able to testify before this subcommittee.

I've been listening to the testimony of the panelists who had preceded me and will try to amplify on some of their comments. I will go a little bit away from my prepared text.

I think the Export Trading Company Act fulfilled a very genuine need in this country to take a more active role in promoting trade. I agree with Ralph Chew and Myron Miller that there are many other initiatives needed. The involvement of the banks is one thing that can be done to help, but other initiatives are also needed.

In light of that perspective, let me comment on what we have done.

First, there was a tremendous amount of imagination and creativity going through the minds of many bankers and businessmen when this law was passed, and I don't think that should be underestimated. It caused many of us to think more about how we fulfill the need of this country to do more trade. That has now died down a little bit, but I think the time is right to come out with some new trade initiatives to get the banks and the exporters thinking again how they can do a better job.

So the promotional aspects of the Export Trading Company Act I don't think should be overlooked.

Chase Trade has done exceptionally well in its first 2 years of operation. We now have several hundred customers and participate in excess of several billion dollars of U.S. export transactions. Most of our activity has been centered on what we would call trade facilitation. Our activity has been extremely profitable, our parent corporation is very pleased with the investment, and we are enthusiastic about our future.

At the outset, we felt that we needed to concentrate on what I will define as the trade process. The trade process includes all of the nuts and bolts, of doing a trade transaction, from financing, to insurance, to transportation logistics, to export licensing, et cetera.

The reason for this initial approach was that this was an area where Chase Manhattan Corp. has enormous expertise. We have a global trade network around the world, and we know the logistics of trade. So we felt that was one area where we could immediately add value and help U.S. exporters.

Second, it was our firm belief that following the model of the Japanese and the Dutch and the Swiss trading companies, this was a long-term exercise; it would not be done in 2 or 3 years, but it would take decades to build the kind of trade networks and trade activities that some of the major trading nations have.

We felt that we needed to build an infrastructure. We had to be able to cope with the logistics of trade, the nuts and bolts of trade, if we were ever to be successful in the more dynamic areas of trading.

And finally we felt that the regulations that we had to operate under were somewhat constraining. And frankly, I don't want to compete in a market where I am at a disadvantage.

What businessmen normally try to do is to find a way to compete where they have the advantage. And where we are going up against very tough international competition, if we are going to be successful, we have to have the tools we need to beat them in markets. This strategy in the short run has served us very well, particularly, given the enormous obstacles that other panel members have cited that we faced after 1982, the strength of the dollar; the debt problems that many of our foreign trading nations incurred, they just could not afford to buy U.S. products.

I would also add that the U.S. economy had recovered far ahead of the European economies. And there was a very strong demand in the United States that fueled imports; there was very weak demand in overseas markets.

So we didn't have the demand to pull the U.S. products during this time when we were trying to set up these trading companies. And it was something new to banks.

There is a strange relationship between bankers and traders. And it does take time to figure out how a trading company can operate within an institutional approach of the bank.

The success factors, as I see them, to these export trading companies are, one, product placing power. And product placing power is a function of overseas distribution networks. It is a function of product knowledge and expertise.

And it is a function of flexibility in trading, whether it is third-country trade, or countertrade, or an import or an export, whatever it is.

Certainly financing is a key ingredient, and not just classical trade finance, but more unconventional techniques of finance, that some of the Swiss and the Dutch have been doing for many years. Good management, we think, is extremely important in getting the kind of talented people that Ralph Chew and the other panelists said were important.

And finally these trade process skills that are outlined. The ability to handle all the trade documentation, and do it well, and do it right.

Now my comments on the Federal Reserve Board's regulations, which I indicated were somewhat inhibiting to our success, will be in light of the success factors on the one hand, and the legitimate concern of the Federal Reserve Board for safety and soundness. I should say that this is also something that was new to the Federal Reserve Board, nobody handed them in 1982 a magic recipe on how to regulate these entities.

But now that we have 3 years of experience, I think it is time to make some regulatory changes. In general, it is our feeling that there should be few rules. There should be as limited rules, and as limited regulations as possible. And the approach of the Federal Reserve should be to look at each company independently, individually, as Mr. Brannen indicated.

It should be based upon the risks inherent in their operation, their experience, their track record, their capital, the markets they are in, the products they are dealing with, as opposed to these across-the-board rules that don't take into consideration the real business that that particular trading company is involved in. It is more difficult, it requires more work, it requires more judgment, but it will allow the trading companies greater flexibility in capturing overseas markets.

I will just quickly go through some of the regulatory things we would like changed. Some of these are really guidelines, or delegation of authority.

They are not iron-clad regulations. But our experience is that when the Federal Reserve System gives a guideline or a delegation of authority criteria, it is almost like moral suasion, people are very reluctant to go in and request exceptions; they are very time-consuming.

They are expensive and require the work of counsel. They are fraught with uncertainty. And there are often conditions attached to them.

So, yes; there is the ability to go back, but we would prefer not to have these rules inhibiting us.

Frankly, we shouldn't even be thinking about the Federal Reserve regulations when we are out there in the marketplace. We should be figuring out how we are going to beat the Dutch, the Japanese and the French; and how we are going to sell products.

And we shouldn't be worried about the regulations. This inventory rule of $2 million is obviously a very arbitrary number. And I can't see how it protects the safety and soundness of an export trading company.

Let me give you an example. A $2 million inventory of shoelaces would be an absurdly high inventory level, and a company that had that inventory in a particular market is likely to suffer some inventory losses. So the $2 million figure alone does not do anything to protect safety and soundness.

On the other hand, just supplying spare parts and tires to heavy equipment, earth-moving equipment, could require millions of dollars in each market in which the trading company is in. So the $2 million is unrealistic and bears no relationship to the market or the product that the export trading company may be dealing in.

The accounting rule for the 50 percent is similarly arbitrary; we believe, that the accounting for the 50 percent should be done in terms of the balance of the U.S. exports to U.S. imports.

If we are going to survive, and be here in the long term to accomplish all of these trade initiatives that we would like to, in the short term we have to be successful, we have to be in many markets. We have to be able to make a profit.

And if we are inhibited from doing third-country trade transactions or countertrade transactions, again, it ties our hands behind our backs competing with foreign competition.

One example is countertrade, we had a transaction where we were taking tractors into Uruguay, United States-manufactured tractors, the concern that was buying these tractors had powdered milk and cheese. They couldn't pay for the tractors. The risks of placing cheese and powdered milk, and the amounts that were required to pay back the tractors made the profit on the countertrade side of the deal five times that of the profit on the tractor sale.

That transaction alone would make it extremely difficult for the trading company to meet the 50-percent rule. And it generates jobs; and it generates tractor sales, and the cheese and powdered milk weren't even coming into the U.S. market.

Section 23A, the application of that fully to the export trading companies is to me the most puzzling of all the regulations. And this may be something that requires changes in the statute as opposed to something the Federal Reserve has the power to change.

But I think what captured the imagination of the Congress in 1982, was this marrying of the strengths of banks, their financing skills, their financing resources with trading, that was what was envisioned. And frankly, it is easier for me to borrow money from First Chicago, than it is to borrow money from Chase Manhattan Bank. And I don't believe that was the intent of the Congress.

In terms of leverage, there are many world-class trading companies that employ much higher degrees of leverage than 10 to 1. Presently Chase trade has a very low leverage. We are now going into phase 2 of our business strategy now that we have a successful base of operation, we have the infrastructure, we have the trade process expertise, we are now getting into a much more aggressive role and building financial assets, doing much more in innovative trade financing.

A 10-to-1 ratio would be totally unrealistic in terms of the business plan that we have right now. We have received an exception from the Federal Reserve. We are able to leverage higher than 10 to 1. But from the first day that we walked across the street to the Federal Reserve bank to explore getting this exception, to the time that it came in, exceeded 11 months.

I wasn't sure we were going to get it approved. My board of directors didn't think we were going to get it. And there are conditions with the exception.

Again, we shouldn't be spending our time thinking about regulations. We should be out there in the marketplace trying to beat the competition.

The export of services is also a very puzzling limitation. It is the one area that the U.S. economy has continued to be strong, despite foreign competition.

We have a trade surplus in many services. And after all, banking organizations are service companies.

We understand the services business. It is the one area we might expect to have a comparative advantage. Where we might be able to teach the Japanese a few tricks; or some of the other foreign competition.

It makes no sense to me to limit the activities of export trading companies to exporting someone else's service. We should be allowed to fully pursue any international service activities that we think are profitable.

After all, what we want from this is U.S. jobs and dollars coming in. And if this creates U.S. jobs, and if this creates U.S. income, it seems to me to be what the act is all about.

So in summary, it is our feeling that the Federal Reserve should remove the inventory rule. They should amend the 50-percent rule.

They should seek a total exemption from section 23A of the Federal Reserve Act.

They should liberalize or totally eliminate the blanket leverage requirement. They should not have any restrictions on the export of services that an export trading company can participate in.

And, finally, they should be more proactive. They could send a different message to the banking community if they were to organize a task force, an office of export trading companies following the very commendable efforts of the U.S. Commerce Department.

It is one thing to have the Commerce Department talking to bankers to try to educate them on how to do trade. Having the Federal Reserve Board, their regulator, explaining how the act works would be better. Explaining the international trade opportunites, doing some staff studies of what banks are doing in other countries to help their industries export.

These would be very positive things. And these would put the Federal Reserve Board in the position of promoting and helping these things to be competitive.

It would send a much different message to the banking community.

Thank you for your time.

Mr. **Barnard**. Thank you, Mr. Rice.

[The prepared statement of Mr. Rice follows:]

STATEMENT OF

R. MICHAEL RICE
PRESIDENT

CHASE TRADE, INC.

ON

THE EXPORT TRADING COMPANY ACT OF 1982

Commerce, Consumer, and Monetary Affairs
Subcommittee
of the
Committee on Government Operations

March 4, 1986

Mr. Chairman and Members of the Committee:

My name is Michael Rice; I am president of Chase Trade, Inc., an export trading company wholly-owned by The Chase Manhattan Corporation. I am pleased to appear today on behalf of The Chase Manhattan Corporation to present our views on the implementation and effectiveness of the Export Trading Company Act of 1982 in regard to bank-affiliated export trading companies.

We feel that the Export Trading Company Act of 1982 filled a genuine need to promote US trade. It is a bill that did not cost the taxpayer anything and has tremendously heightened awareness of export trade in the American banking and business communities. It prompted us all to think more creatively about export finance and the facilitation of international trading opportunities for U.S. corporations.

Approximately 40 banks now have affiliated export trading companies. Dozens of industrial corporations have also utilized the anti-trust provisions of the Act. In the short term, these initiatives and new ideas have translated into many new jobs. In the long term, we are equally hopeful about the potential opportunities for bank-affiliated trading companies to increase American exports of goods and services as they develop a strong partnership with U.S. exporters.

The export trading company has thus far been an excellent investment for The Chase Manhattan Corporation. With three offices in New York City, Delaware, and in the Virgin Islands, Chase Trade has pursued a strategy that concentrates on the facilitation of trade.

In its first two years of operating experience, Chase Trade has been highly successful with this strategy. We have in excess of 350 customers, and transactions in which we will participate should exceed several billion during 1986. The affiliation with The Chase Manhattan Bank, N.A. has been of enormous value in our effort to expand the business, and we look forward to continued growth of our export trading company activities.

During these start-up years, I would like to emphasize that Chase Trade has chosen not to concentrate a large portion of its efforts on the direct sale of goods. In contrast to other bank-affiliated export trading companies, we have spent a majority of our time on services that facilitate trade - on financing, insurance, transportation logistics, documentary services, and other trade activities that we refer to as the "trade process." The reasons for concentrating on this market are three-fold:

First, trade finance is an area where Chase has great expertise, and the trading company enhances our traditional trade finance tools. Drawing on our expertise in this area Chase Trade is establishing a reputation with corporations for its ability to add value in trade transactions through its offering of trade facilitation services.

Second, we recognized the need to build a solid base and infrastructure before significantly expanding into the more commercial aspects of trading. A trading company must have strong expertise in the trade process if it hopes to be a successful trader.

Third, we feel that the current Export Trading Company regulations would hurt us competitively as a bank-affiliated export trading company if we expand beyond trade facilitation. When we go up against formidable foreign competition, we want to have equal or better ability to compete.

This strategy of concentrating on trade services has served us well given the enormous problems export trading companies have encountered since passage of the Export Trading Company Act.

From a business point of view, it is difficult to imagine a more adverse set of economic forces to be confronted with when developing a new business:

- The well-publicized strength of the U.S. dollar from 1982 through 1985, placing U.S. goods at a price disadvantage in most markets around the world.

- The international debt problems experienced by many of our trading partners, making it difficult for them to pay for U.S. goods.
- The strength of the U.S. economy, creating a demand for imported products in the U.S., contrasted to weaker economies and weaker demand for U.S. goods abroad.

These factors need to be placed in context of the normal challenges that are to be expected when starting any new business. Export trading companies represent a very new business for bankers, and a start-up period is usually needed to develop market experience. Most of us knew at the outset when the Export Trading Company Act took effect that it would be difficult for bankers who trade the most fungible of all commodities - money - to make the leap and begin to participate in the trade of commercial goods.

Thus, it is not surprising, given the formidable economic obstacles and the normal difficulty in establishing a new business, that the export trading company industry has not yet realized its potential. Fortunately, the outlook is now much more positive, particularly in view of the recent drop in U.S. dollar exchange rates.

In my view, the key "Success Factors" for an export trading company are:

- Product placing power, a function of overseas distribution networks and product knowledge, and flexibility to participate in a variety of trade flows.

- Access to financing, including unconventional financing when needed to ensure the ability to compete effectively.
- Good management
- "Trade process" knowledge and capabilities.

The Subcommittee has asked our views on the Federal Reserve Board regulations on export trading companies and how they promote or inhibit success. Our comments take into consideration both these key "Success Factors" and the Federal Reserve's legitimate concern for bank safety and soundness. It is, therefore, appropriate to ask two questions. Do the regulations provide the flexibility for an export trading company to succeed? At the same time, do the regulations effectively ensure a sound operation?

FEDERAL RESERVE BOARD PROMOTION AND REGULATION OF BANK EXPORT TRADING COMPANIES

The Federal Reserve Board has been given the dual mandate to promote and to regulate bank-affiliated export trading companies. The tasks of encouraging the export trading company business and, at the same time, setting restrictions through regulation are, to some degree, a strained partnership.

The Export Trading Company Act was a new area for banks and for the Federal Reserve in 1982. Now, we have the benefit of three years of experience with export trading company activity. Based on that experience, we believe that the current regulations should be liberalized to capture the spirit of the statute (Title II of the Export Trading Company Act of 1982). If unchanged, the regulations will hinder the successful development of bank-affiliated export trading companies.

The clear Congressional mandate to the Federal Reserve was to encourage and assist the growth of export trading companies by providing "for the establishment of export trading companies with powers sufficiently broad to enable them to compete with similar foreign-owned institutions in the United States and abroad" (Section 202(1) of the Export Trading Company Act of 1982).

We recognize that this competitive mandate must be balanced with the important considerations of bank safety and soundness. However, we feel that the safety and soundness concerns of the Federal Reserve should be dealt with on a case-by-case basis with each individual bank-affiliated export trading company rather than by across-the-board rules. The statute has prudential limits on the amount of capital and financing that a bank holding company or affiliated bank can make available to a trading company. In addition, the Federal Reserve has the authority to examine export trading companies. We believe that these prudential limits and the examination authority provide the Federal Reserve with sufficient means to ensure the safety and soundness of the affiliated banks.

The following are some specific regulatory and policy positions that hinder the growth of bank-affiliated export trading companies:

1. Inventory Rule: The Federal Reserve generally limits to $2 million the value of goods to which the export trading company can take title without a firm order for resale (Rules Regarding Delegation of Authority, 12 CFR 265.2(f)(46)). This arbitrary limit reduces the export trading company's trading flexibility and substitutes the Federal Reserve's judgment on appropriate inventory levels for the more experienced judgment of export trading company management. The rule does not help in fulfilling the "Success Factors" nor does it effectively bring about safety and soundness.

For example, a $2 million inventory of shoe laces would probably be an absurdly high level of inventory for any given market. In strong contrast, a $2 million inventory of replacement parts for a large project of heavy equipment might be woefully inadequate to supply customers promptly. One Off-Highway Truck Tire for mining equipment could cost in excess of $100,000. In every market where such equipment is being sold, a reasonable number of such tires would be needed, not to mention other items.

We believe that trading companies should be permitted to take title to any quantity of goods irrespective of whether there is a firm order for resale. Naturally, the trading company itself will impose appropriate limits dependent on the type of product and market conditions.

2. Counting revenue under the 50 percent rule: The Federal Reserve Board regulations require a bank-affiliated export trading company to derive more than 50% of its revenue from U.S. exports or from the facilitation of U.S. exports in any two-year period (12 CFR 211.32(a).

This requirement has a reasonable foundation. However, we believe that the accounting for the 50% rule should include only the value of U.S. exports and U.S. imports. If bank-affiliated export trading companies are to be profitable, they must have full flexibility to engage in third country trade.

The manner in which the Federal Reserve currently considers revenue for the 50% rule is neither necessary to satisfy the legislative mandate of promoting U.S. exports nor necessary to ensure the goal of safety and soundness, but it conflicts with the Success Factors. Furthermore, countertrade arrangements have grown increasingly important in the conduct of international trade and often provide the only mechanism whereby a U.S. exporter can gain access to certain overseas markets. The current rule serves to inhibit countertrade.

For example, assume that a bank-affiliated export trading company facilitates the export of a U.S. product, takes foreign goods in countertrade as payment, and earns a fee of $250,000 for the entire transaction. The Federal Reserve regulations are unclear as to whether the fee on this type of transaction is required to be allocated between the export and the countertrade parts of the transaction. The allocation of more than half the fee to the countertrade part of the transaction would actually hinder the export trading company from meeting the 50 percent revenue test, even though the countertrade allowed an export transaction to go forward which otherwise might not have occurred at all and even if the countertrade goods were not a U.S. import.

We believe that because a transaction of this type is based upon a U.S. export transaction, the entire fee should be considered as export-related revenue. At the very least, the export trading company should not be penalized by a negative treatment of the countertrade part of the transaction.

We recommend that the Federal Reserve adopt a rule that only requires U.S. export revenue to exceed U.S. import revenue.

3. Application of Section 23A: In an apparent conflict with the intent of Congress as evidenced in the Conference Report, the Federal Reserve is imposing certain collateral requirements of Section 23A of the Federal Reserve Act on the borrowings of export trading companies

from affiliated banks. A major premise behind allowing bank holding companies to invest in export trading companies was the use of the bank's financial resources and know-how to stimulate export transactions. It was explicitly stated on page 20 of Conference Report that 23A would not apply.

The collateral requirements, as they stand, limit the ability of the bank to bring its full financial resources to the export trading company. In addition, by including export trading company financing in the 23A pool, the trading company must compete with other non-bank affiliates for the bank's limited financing resources available to affiliates by 23A. The Federal Reserve should substantially broaden the limited exemption from the collateral requirements in 12 CFR 211.33(b)(3) or consider a total exemption from Section 23A.

4. Asset-to-capital leveraging ratio: The Federal Reserve generally limits a bank-affiliated export trading company to a debt-to-capital ratio of not more than 10 to 1. (Rules Regarding Delegation of Authority, 12 CFR 265.2(f)(46)). This arbitrary figure does not permit us to employ the same degree of leverage customary with many trading companies not affiliated with U.S. banks, and consequently places us at a competitive disadvantage.

Foreign trading companies frequently have ratios in excess of 20 to 1. Upon examination, if the Federal Reserve believes that a specific export trading company's leverage has an adverse impact on an affiliated bank, the Federal Reserve can easily limit that trading company's leverage as part of its supervisory oversight.

As with inventory, the Federal Reserve has somewhat arbitrarily substituted a blanket rule for the judgment of trading company management on the proper leverage needed for competitiveness and profitability. It does grant waivers; in fact we have received approval to leverage beyond 10:1. But, the approval process often is lengthy and frought with uncertainty.

We recommend no less than a 20 to 1 leverage ratio guideline, if one is needed at all. Again, in terms of safety and soundness, we believe that bank-affiliated export trading companies must be evaluated individually, based on their track record, the risks in their operation, the strength of the parent, and other business factors.

5. Additional Investments: Currently Federal Reserve Regulations require prior notification for a bank holding company to make additional investments in an export trading company. Since export trading companies will grow over time and require many additional capital investments to support such growth, a more flexible approach would be to merely require a notification of the additional investment after-the-fact. Of course, this assumes no change in the activities that the Federal Reserve originally approved.

6. Export of services: Congress did not want bank-affiliated export trading companies to engage in manufacturing or in agriculture, and said so clearly in the statute. But, Congress also stated on page 23 of the Conference Report on the Export Trading Company Act of 1982 (Section 103(a)(2)) that it did not intend to limit the services offered.

Bank-affiliated export trading companies possess distinct comparative advantages in dealing in services, and trade in services is as important to our future balance of trade position as trade in goods.

Clearly, looking at the historical trade data below, the U.S. has an historical surplus and comparative advantage in trade in services, excluding shipping. While the balance on merchandise trade has fallen from a $2.6 billion surplus in 1970 to a $114 billion deficit in 1984, the balance for services has risen nearly 450% from $2.2 billion to $9.8 billion during the same period. This is the area where banks have the most expertise and bank-affiliated export trading companies might be expected to have the most success.

U.S. INTERNATIONAL TRANSACTIONS

(Millions of Dollars)

	1970	1980	1984
Merchandise Trade Balance	2,603	(25,480)	(114,110)
Net Investment Income	6,231	30,386	19,109
Net Military Transactions	(3,354)	(2,237	(1,765)
Net Travel & Trans. Receipts	(2,038)	(997)	(8,974)
Net Other Services	2,180	7,277	9,791
Balance on Goods & Services	5,624	8.950	(95,945)
Net Unilateral Transfers	(3,294)	(7,077)	(11,413
Balance on Current Account	2,330	1,873	(107,358)

In a manner that is more restrictive than the statute and is inconsistent with the legislative history, Federal Reserve regulations prohibit a bank-affiliated trading company from exporting its services (12 CFR 211.32(a)). We recommend that the Federal Reserve remove this impediment. The rule certainly is not necessary for safety and soundness.

Again, while the Federal Reserve will consider waivers from all of the above regulations, experience indicates the exceptions are often difficult to obtain and require considerable time to process, all of which creates business uncertainty.

Turning from regulations to the broader objective of the development of export trading companies, we have the following comments.

We recommend that the Federal Reserve Board, along with the Commerce Department, assist in the successful development of export trading companies by giving banking organizations the support they need to become active players in the international trade arena. We, therefore, suggest that the Federal Reserve Board establish an Office of Export Trading Companies. This proposal need not entail new staff hiring but rather could be a task force of existing staff concerned with international bank activities.

The mandates of the Federal Reserve's Office of Export Trading Companies would include:

- Education of the Federal Reserve staff, including Reserve Bank staff, in international trade practices and techniques.
- Seminars to educate banking organizations in the role an export trading company could play to support U.S. exports through an export trading company.
- Establishment of a "hot line" to ensure quick response to questions on interpretations of regulations and, particularly, the granting of waivers.
- Staff studies and analysis of bank support of export trade in other countries with recommendations on areas where U.S. banking organizations could expand their roles.

We believe that a Federal Reserve effort in this area would be more effective with bankers than the commendable efforts of the Commerce Department alone.

In conclusion, we feel the Federal Reserve should amend its regulations on export trading companies as we have suggested:

1. Remove any limit on inventory positions.
2. Amend the 50% rule to require only that U.S. export revenue exceed U.S. import revenue.
3. Exempt export trading companies from Section 23A of the Federal Reserve Act.

4. Liberalize or eliminate the asset-to-capital leveraging ratio.
5. Institute post-notification on additional investments.
6. Allow unrestricted export of services.

Overall, we are very pleased with the Export Trading Company Act. Three years ago, very few of us could envision the role bank-affiliated export trading companies would play or how strongly they could support U.S. exports. The Act has proven to be creative and beneficial legislation, and with these regulatory changes, we may be able to realize the full potential envisioned in 1982.

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Mr. **Barnard**. Your testimony, both of your testimonies, have certainly prompted a lot of questions that we need to explore. I am probably going to take advantage of the opportunity of asking you to respond to some questions in writing, if you would be so cooperative to do so.

Gentlemen, first of all, you have heard Senator Heinz testify this morning; are you familiar with his bill?

Mr. **Brannen**. Yes, sir.

Mr. **Barnard**. Do you think his bill would, No. 1, correct all the problems that you have? And, No. 2, do you have additional items that you would like to see addressed, Mr. Brannen?

Mr. **Brannen**. I think that the one area where his solution is not ideal is in the leverage-ratio area.

Mr. **Barnard**. You mean the 10 to 1?

Mr. **Brannen**. Yes.

Mr. **Barnard**. You want the 25 to 1, I believe?

Mr. **Brannen**. But I believe the way he did it was such that the Federal Reserve could still delay approval. What the legislation says, as I understand it, is that they may not deny a 25-to-1 ratio for that reason only. But as a regulator they could find a lot of other reasons to ask a lot of questions and delay approval of the leverage ratio of 25 to 1.

We would like to suggest that they be instructed not to initiate leverage ratios of less than 25 to 1 unless they find something wrong with the company. It is just a little different approach to solving the problem. We think it would be a better solution.

Mr. **Barnard**. Mr. Rice.

Mr. **Rice**. I think that Senator Heinz' bill is right on target in terms of the banking aspects of this. I do believe that there is a lot more work that needs to be done thinking about the Eximbank.

I do believe also that Myron Miller and Ralph Chew are correct, that we have a trade crisis; that there are many other initiatives that we have to think about. The bank ETC's alone are not the answer.

It is one positive thing. It is one initiative that can be done that doesn't cost the taxpayer anything. There are many other things that I think have to be considered that go beyond the Heinz bill.

Mr. **Barnard**. I know that when we were considering the bill in 1982 that we have now enacted, there was a lot of discussion about the antitrust provisions. I am not saying that we need remove those. But have those antitrust provisions really done a lot for forming ETC's or affected the operation of ETC's?

Mr. **Brannen**. I don't believe so, no. And certainly on the banking side we don't see where they are of great use to us in our activities. I know that there have been discussions in some of the industry trade groups about forming ETC's and utilizing those provisions. But in general, competitors are competitors and they find it difficult to get together in that kind of an environment.

Mr. **Rice**. I would think, if I could add to that, that by their very nature that banks are utilities. We provide financing and services to a broad customer base. So we generally don't have an antitrust problem.

I do think that when the Chlor-Alkali antitrust certification was issued, which was an extremely large certification, there was a feeling in the export community that this was going to be positive, and that there would be quickly coming onstream a lot more certifications from larger companies. And I think this recent court decision has thrown some ice water on that.

Mr. BARNARD. Gentleman, the Export Trading Company Act was primarily established to assist small- and medium-size businesses to export. Now you were here this morning when we heard from Mr. Hammonds, on how he could not get help from two banks, and so forth; we also know that a local bank will not touch an export product transaction that is worth less than $1 million in value. Do you have a limit on size of a business that you will help?

Mr. BRANNEN. We do not. In fact, most of the transactions we have entered into have started very small, less than $100,000, but we obviously hope they have potential for growth over a period of time. Or that we can service a whole lot of little transactions in a given market, so that we get some economies of scale.

Mr. BARNARD. Well, gentlemen, again, I want to say that we have some additional questions we would like to pose to you in writing; your testimony has been excellent. And, of course, as I stated in the outset our real function today is to have oversight hearings on the Export Trading Company Act, as it is regulated, and administered, and serviced by the Department of Commerce and the Federal Reserve Board.

We could get into long and elaborate discussions today of why we are not competing in foreign markets. And I think it is very important that we do so. I have, as just one Member of Congress, some very definite ideas that we are going at it in such a piecemeal fashion and that we are really not taking in the whole picture at any one time.

I know; I was very involved in the textile legislation, which you can understand, considering where I come from in the country. But there again, that is in and of itself, a limited correction. I mean, we have got to look at this entire process. And as someone brought out, and I think it was Mr. Chew, we have just got to basically redirect our domestic manufacturers and service organizations toward exports. We are just not inherently directed toward that. And it is going to be a long process, but we need to do that.

And, of course, I think the Export Trading Company Act was a small, small incentive to try to move a big, big problem. And, of course, we are all disappointed with the fact that we haven't done it. But yet, it has possibilities, and with a massaging and correction, I think, we can improve that.

Mr. Brannen, I am sorry I didn't meet you before because I paid $68 for that talking bear. Now if you can tell me where I can buy another one for $24, I would be glad to buy several.

Mr. BRANNEN. You have to add as many dollars to the economy as possible.

Mr. BARNARD. That is the most amazing bear I have ever bought.

Well, gentlemen thank you very much for being with us today. And thank you for your testimony, I am sure it will be very helpful.

[Submissions to additional subcommittee questions follow:]

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James S. Brannen
Senior Vice President

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COMMERCE, CONSUMER AND
MONETARY AFFAIRS SUBCOMMITTEE

April 11, 1986

Honorable Douglas Barnard, Jr.
Chairman
Commerce, Consumer and Monetary
Affairs Subcommittee of the
Committee on Government Operations
Rayburn House Office Building
Room B-377
Washington, D.C. 20515

Dear Congressman Barnard:

This is in response to your letter of March 21, 1986 requesting certain information amplifying my testimony given at your Subcommittee's hearing on the Export Trading Company Act on March 4, 1986. For purposes of format I will repeat the questions you posed and then attempt to answer them.

1. "On page 5 of your written statement, you indicated that it is no coincidence that most 'successful trading companies have developed where the domestic market opportunities were limited.' What are those areas? Could you give us some examples?"

   I had in mind places such as Holland, Japan, Hong Kong and Singapore. These are all countries which have long histories in world trade. They are countries which need to import raw materials because they lack plentiful natural resources and in most cases they must export finished goods due to the relatively small size of their domestic markets. Equally important, these are all countries where government policies promote exports and where government actively supports and encourages the development of export industries.

2. "Have bank ETCs been placed at a competitive disadvantage with nonbank ETCs, because of the Federal Reserve Board's rules? If so, please describe the specific disadvantages, giving examples if possible."

   Yes. Non-bank ETCs operate in the free marketplace with essentially no regulatory burdens. As a result, any regulations which are imposed on bank ETCs serve to make their operations either less efficient because of costs associated with regulations or less responsive than their non-bank competitors. In my testimony I cited several specific examples of regulations imposed on bank ETCs which served to put them at a disadvantage. These regulations are the 50% rule, the imposition by the Federal Reserve Board of asset/capital ratios, the regulatory requirements of Section 23 A of the Federal Reserve Act as they apply to ETCs and the regulatory interference with an ETCs freedom to determine its own inventory policies. ETCs not owned by banks are regulated by competitive pressures, internal policies and the dictates of the marketplace. Imposition of all of the above-cited regulatory requirements on bank ETCs places them at a competitive disadvantage in attempting to grow their businesses.

3. "(a) What types of restrictions do the Japanese and Western European Governments place on their bank export trading companies and how do they differ from the Federal Reserve Board's regulations?

   (b) Also, to the extent known, what types of specific subsidies do these governments confer on the ETCs?"

   I have no specific information to provide in answering these questions nor am I readily familiar with a source for obtaining such information.

4. "A number of bank ETCs have been closed or are otherwise dormant. Other than the problems with the overvalued dollar, please set forth your views as to the reasons for this situation. (a) For example, have bank ETCs moved too fast in setting up distribution networks and trying to find markets? (b) What types of mistakes have they usually made? (c) On the other hand, have parent banks of less-than-successful ETCs not devoted adequate resources or manpower to their ETCs, not making the long-term commitment necessary? (d) What should a parent bank expect?"

   (a) It appears that bank ETCs have very little to show today in the way of distribution networks. Rather than having moved too fast they may have moved too slow when they recognized the cost of building overseas distribution. I do not believe that the present level of inactivity among bank ETCs can be attributed to mistakes made by investing at a pace which exceeded their ability to assimilate such build up.

   (b) I believe that a number of bank ETCs originally had strategies directed toward development of a significant countertrade capability. Most banks that began with such a focus found it more difficult to pursue than they had originally envisioned, and, in view of the difficulties of developing export trade in today's environment have chosen to stand by for the time being and not make additional investments until the trade picture has improved and the regulatory environment has been clarified.

(c) I have no knowledge of parent bank attitudes other than those of First Chicago Corporation, and it is my belief that First Chicago has appropriately taken a long term view toward their commitment to ETCs. On the other hand, my impression is that some banks set unrealistic short term profit expectations for their ETCs rather than take a long term view toward building a business.

(d) As I pointed out in my testimony, the trading company business is a low margin business and any parent bank should expect only small profits which can grow gradually over time. In addition, if they elect to form a wholly-owned ETC they should expect to invest significant capital in the development of their distribution networks.

5. "You and other witnesses referred to the natural incompatibility between banking and trading. One person told us that bankers and traders do not think alike and operate differently. And several witnesses alluded to this. How do we overcome this gap? How much of the lack of success originates from this conflict?"

The differences I alluded to arise from the differences in risk associated with trading in financial assets and trading in merchandise. When one trades in financial assets the risk assumed is that the obligor will not be able to pay when the due date comes, and the result of accepting this risk under such circumstances is frequently the loss of most of the money loaned or invested. On the other hand, when one trades in merchandise there is flexibility to sell the goods to some other party and to recover a substantially greater portion of the investment. Thus, a trader of merchandise is able to take a number of interim steps to cut potential losses whereas the banker dealing in financial assets does not have the same degree of flexibility. Bankers seem to have great difficulty embracing the concept of merchandise risk.

The best way to overcome the gap between the thinking of bankers and merchandise traders is for the banks to have partners in their ETCs who have mercantile backgrounds and who have installed systems to approve the risks associated with the extension of trade credit and other risks associated with taking title to goods. The fact that most banks have not adopted this strategy might well have contributed to the lack of success most ETCs have experienced.

I hope this letter is responsive to your questions and that my observations will be helpful to you and your staff. Please feel free to contact me if I can be of further assistance.

Sincerely,

James S. Brannen
Senior Vice President

JSB/11

Irving Trust

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The Honorable Doug Barnard, Jr.
Chairman
Subcommittee on Commerce, Consumer, and
Monetary Affairs
Committtee on Government Operations
Rayburn House Office Building
Room B-377
Washington, D. C. 20515

March 27, 1986

Dear Mr. Chairman:

This is in reply to your letter of March 21 regarding my testimony at the March 4 hearing on the Export Trading Company Act. First, as you can see from the letterhead, I have just joined Irving Trust Company, so I will be relating to you past experience from my former firm. In response to your specific questions:

Question 1: In my written statement I made the point that I, as a bank ETC, want to have an "equal or better ability to compete" and that the Federal Reserve's regulations have hurt me competitively. You ask that I elaborate on this statement. For example, what types of competition am I referring to--foreign bank export trading companies or American nonbank ETCs? What are the specific competitive advantages I have encountered, which other entities are involved, and, if possible, could I give some examples.

Answer: In terms of competition, I was referring principally to foreign trading companies, whether affiliated with banks or not. Some of the most successful trading companies are the well-established Swiss, Dutch, British and Japanese companies. In my statement, I indicated that the Federal Reserve's Regulations would put us at a competitive disadvantage with these companies if we were competing in their markets. In fact, as I indicated, we had not been harmed by this because in Phase I of our operation, we concentrated on building our operating infra-structure, providing documentary services, trade facilitation services and financing. Phase II of our planned expansion

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COMMERCE, CONSUMER AND
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would take us into direct competition with the world class competitors and it is at this point that we would be at a disadvantage. Specifically, all those regulatory obstacles listed in my testimony are not obstacles for the foreign trading companies. They are free to conduct their business affairs in whatever manner necessary to penetrate markets. Their competitive advantage is simply a lack of arbitrary and constraining rules.

Question 2a: What types of restrictions do the Japanese and Western European Governments place on their bank export trading companies and how do they differ from the Federal Reserve. Board's regulations?

Answer: I am not aware of any restrictions placed on foreign trading companies other than the laws and regulations of the country which all companies doing business in the country must comply with.

Question 2b: To the extent known, what types of specific subsidies do these governments provide their ETCs?

Answer: Other than export credit agency financing, insurance and guarantee schemes which all exporters in a given country may be eligible for, I am unaware of any special subsidies made available to ETCs.

Question 3: Other than the problems with the overvalued dollar, please set forth views as to the reasons for the fact that a number of bank ETCs have been closed or are otherwise dormant. For example, have bank ETCs moved too fast in setting up distribution networks and trying to find markets? What types of mistakes have they usually made? On the other hand, have parent banks of less-than-successful ETCs not devoted adequate resources or manpower to their ETCs, not making the long-term commitment necessary? What should a parent bank expect?

Answer: Since the ETC I formerly headed was quite successful, I can only give impressions as to why some of the other bank ETCs have not performed up to expectations. Most significant I believe they vastly underestimated the time and resources required to build distribution networks. I think many lacked a clear market and product focus and did not sufficiently capitalize on strengths unique to their organizations. You mentioned the strength of the dollar which was an enormous obstacle. In addition, those newly emerging markets that would generally represent new trade opportunities were predominantly associated with countries experiencing severe debt problems and strict import restrictions. In addition, the U. S. economy recovered well ahead of many of our trading partners fueling imports in this country without a concomitant demand from abroad for U. S. goods.

Finally, as you suggest, the long-term commitment may not have been strong enough from the parent company to see these struggling ETCs through all of the obstacles discussed at the March 4 hearings. A parent bank holding company realistically should probably have a five year time horizon for the development of export trading companies.

Question 4: Regarding the natural incompatibility between banking and trading, it has been suggested that bankers and traders do not think alike and operate differently. How do we overcome this gap? How much of the lack of success originates from this conflict?

Answer: I think the simplest solution is to get the right type of management in the ETC. If the key executive(s) on the ETC is (are) comfortable in a banking environment yet fully knowledgeable in the dynamics of trade, the two disciplines of banking and trading can be complementary. It's a function of management in my view.

Sincerely,

R. Michael Rice
Executive Vice President

Mr. **Barnard**. Our next panel will represent the Department of Commerce and the Federal Reserve Board. I would like to ask Mr. James V. Lacy, Director of the Office of Export Trading Company Affairs, and Mr. Frederick R. Dahl, Associate Director, Division of Banking Supervision and Regulation of the Federal Reserve Board, if they would come forward.

Gentlemen, we appreciate your being with us today. And, again, I want to thank you for your patience for sitting through these hearings. I hope that the testimony that you have heard has been interesting, as well as edifying and, hopefully, that you can respond to some of the observations that have been made about the Export Trading Company Act.

Mr. Lacy, we formally welcome you as the Director of Office of Export Trading Companies, and hope that this will be a long and profitable tenure on your part. And we hope to see you often at these hearings, as part of our oversight. So, we will hear from you first.

STATEMENT OF JAMES V. LACY, DIRECTOR, OFFICE OF EXPORT TRADING COMPANY AFFAIRS, U.S. DEPARTMENT OF COMMERCE

Mr. **Lacy**. Thank you, Mr. Chairman.

Mr. **Barnard**. You might want to pull the microphone close to you, sir.

Mr. **Lacy**. How is that?

Mr. **Barnard**. That is better.

Mr. **Lacy**. We have a prepared statement which we would like to submit.

Mr. **Barnard**. Without objection, we will accept the full testimony; and we would appreciate if you could summarize.

Mr. **Lacy**. Mr. Chairman, I appreciate the opportunity to comment on the GAO report, and report on Commerce's implementation of the Export Trading Company Act. We appreciate the thorough review that GAO conducted regarding the ETC Act. And as we have stated in the record, we are in agreement with the conclusions of the report.

The Export Trading Company Act of 1982 was viewed at the time of its passage by Congress as a landmark piece of legislation, which sought to increase U.S. exports by removal of antitrust disincentives, to export activities, and to regulation of the banking industry to provide new business opportunities through exporting. By the end of February 1986, Commerce, with the concurrence of Justice, had issued 62 antitrust certificates of review providing antitrust protection to 259 firms and individuals.

As has been stated, 40 bank holding companies have made investments in 38 bank export trading companies in that time. While expectations surrounding Congress' passage of the ETC Act were high, as has been noted in the course of these hearings, we feel there is ample reason to believe the ETC Act has been a useful tool in promoting U.S. exports, and, given more experience with the act, it will provide a means for greater expansion of U.S. exports in the future.

The bank holding company investments in ETC's have totaled about $84 million. In addition, the fact that 259 firms and individuals are participating in our Commerce certificates demonstrates the fact that the act is being used.

But Commerce would like to see the act used even more widely. As the GAO report notes, the export environment during the past few years has been difficult, particularly because of the high value of the dollar against the currencies of foreign countries.

But the Department has encountered some obstacles other than the high value of the dollar in promoting use of title III. Aside from the fact that many U.S. firms don't believe that export operations that they are engaged in raise antitrust concerns, some companies have deferred seeking a certificate of review until the value of the certificates protection has been clearly demonstrated.

Application for a certificate entails disclosure of certain proprietary information to both the Departments of Commerce and Justice. Some members of the private antitrust bar, for example, have taken a wait-and-see attitude.

They have counseled their clients to exercise caution in disclosing business plans notwithstanding the confidential nature of such disclosure.

In addition, some businesses may be relying on title IV of ETC Act, which amends the Sherman Act and section 5(a) of the FTC Act, to clarify those antitrust statutes with respect to jurisdictional issues. To benefit from title IV does not require a filing or an application with the Commerce Department or the Justice Department.

Nevetheless, Commerce is pursuing an active effort, under its title I responsibilities, to promote use of the act. This year, for example, Commerce is conducting nine national conferences in cooperation with our district office network.

One of the conferences, I might add, will be in Mr. Hammond's area in Pittsburgh and is being supported by our Pittsburgh district office.

Our promotion for these conferences includes a total of 84,000 pieces of mail to firms that we have identified that might be likely participants at the conference. Other trade development issues besides the ETC Act will also be discussed at the conferences.

Beyond that, Commerce is actively engaged in conducting conferences and outreach efforts targeted to the public sector, agricultural cooperatives, the banking community, shippers associations, Webb-Pomerene Associations, and other sectors where our internal analysis indicates the act could be useful to improve exports. Another important part of the Department's responsibility to promote ETC's has been the establishment of a Contact Facilitation Service available through any of Commerce's 47 district offices.

The CFS is designed to facilitate contact between U.S. producers of goods or services and firms offering export trade services. Companies or individuals who wish to form an ETC may also use the CFS to identify others who are interested in establishing an export trading company.

Our earlier experience with this program resulted in the development of a format and data base which was published in the form of a directory entitled "Contact Facilitation Directory." We had over 1,700 firms appear in that first edition representing something along the lines of 3,000 product lines.

That directory was published in June 1984. In September 1985, we sent out a brochure with a registration form to 55,000 firms throughout the United States, which we identified as likely small- and medium-size firms to participate in such an endeavor.

The lists were compiled not only from Commerce lists, but from a commercial list broker and also from the Small Business Administration. The second edition of this directory, to be entitled "Partners in Export Trade," will provide a listing of more than 4,000 firms this time with entries representing every State.

The publication is scheduled for June, and distribution to the public will be through sales by the Government Printing Office. The Department of Commerce also will engage in an active promotional campaign.

Over the past 2 years our promotional program has become somewhat more targeted to those sectors of the business community that our analysis has indicated are the most likely beneficiaries of the ETC Act. It is not possible to identify ETC's that might have been formed directly as a result of our promotional efforts.

But we are aware of many instances in which exporters in those groups targeted have subsequently applied for a certificate of review, for example. A specific point would be that many of the Federal Reserve Board bank ETC's have attended one or more of our bank conferences.

We believe our outreach efforts directed toward Webb-Pomerene Associations, shippers' associations, and agribusiness firms have been successful in stimulating use of the certificate of review program. Several certificates have been issued to groups belonging to Webb-Pomerene Associations. Two recent applications from shippers' associations are in the works, they are being processed by our office.

More certificates involving collective export activities have been issued to agribusiness concerns than any other industry group. It should be noted that the act contains no requirement that a nonbank ETC identify itself through some form of registration or licensing procedure.

Contrary to the impression held by many, the benefits of the act are available to all exporters, not just ETC's. Any firm can use the Contact Facilitation Service.

Any exporter can apply for section 206 working capital loan guarantee from the Eximbank. And any person can apply for a title III certificate of review, not just an export trading company.

Furthermore, the clarification of U.S. antitrust laws jurisdiction provided by title IV, again, extends to all exporters.

With respect to the Contact Facilitation Service directory we are pleased that is moving up from 1,700 listings in the first edition to more than 4,000 in the forthcoming second edition. And we feel that is an indication of the continuing vitality in our outreach efforts.

Our office believes the internal assessment of our title I programs together with public feedback provide a reliable indication about which efforts are the best use of our limited promotional resources. We have used conference evaluations to critique both speakers and subject matter. And we critique ourselves after each conference and after each title I promotional activity.

We are looking forward to continuing new applications into our ETC office and continuing new potential uses of the act.

Thank you, Chairman, that completes my remarks.

[The prepared statement of Mr. Lacy follows:]

Prepared Statement of James V. Lacy

Director, Office of Export Trading Company Affairs

International Trade Administration

U.S. Department of Commerce

Before the

Commerce, Consumer, and Monetary Affairs

Subcommittee

of the

Committee on Government Operations

March 4, 1986

Mr. Chairman and members of the Committee, I am James V. Lacy, Director of the Office of Export Trading Company Affairs, International Trade Administration, U.S. Department of Commerce. I am pleased to have this opportunity for the Commerce Department to address the General Accounting Office's draft report concerning the Export Trading Company Act and to report on Commerce's role in implementing the Act.

The Export Trading Company Act of 1982 was viewed at the time of its passage by Congress as a landmark piece of legislation which sought to increase U.S. exports by encouraging more efficient provision of export trade services to producers and suppliers, improve the availability of trade finance, and remove antitrust disincentives to export activities. Its principle provisions give authority to bank holding companies, Edge Act banks and bankers' banks to own all or part of an ETC, and provide the American business community with the opportunity to obtain an antitrust preclearance for export operations.

As of the end of February 1986, the Commerce Department, with the concurrence of the Department of Justice has issued 62 antitrust certificates of review which provide antitrust protection to 259 firms and individuals. In addition, the Federal Reserve Board has approved investments by 40 banks in 38 bank export trading companies.

While expectations surrounding Congress' passage of the ETC Act were high, there is ample reason to believe that the Export Trading Company Act has been a useful tool in promoting U.S. exports, and given more experience with the Act, it will provide a means for greater expansion of U.S. exports in the future.

As the General Accounting Office report notes, the export environment during the past few years has been difficult, particularly because of the high value of the dollar against the currencies of foreign countries. But, the report also noted that the increased awareness toward exporting could result in the formation of many more ETCs, and in increased export trade.

Aside from the fact that many U.S. firms do not believe their export operations raise antitrust concerns, some companies have deferred seeking a certificate of review until the value of the certificate's protection has been clearly demonstrated. Application for a certificate entails disclosure of certain proprietary information to the Departments of Commerce and Justice. Some members of the private antitrust bar have taken a "wait and see" attitude, and have counseled their clients to exercise caution in disclosing business plans notwithstanding the confidential nature of such disclosure.

Another reason might be that some businesses are relying on the protection of Title IV which amends the Sherman Act and Section 5(a) of the FTC Act to clarify that these antitrust statutes do not apply to export trade unless there is a direct, substantial and reasonably foreseeable anticompetitive affect on domestic commerce.

Title I Activities of the Office of Export Trading Company Affairs

OETCA engaged in an active promotional effort for the Export Trading Company Act in 1985, and has plans for an extensive, national effort in 1986.

Promotion Efforts in 1985

In 1985, OETCA continued to cosponsor conferences with professional groups, such as major national accounting firms, to promote the ETC concept and use of the Title III antitrust provisions. Cooperative efforts with such groups has resulted in cost savings to the Government for ETC Act promotional expenses. Conferences and outreach programs oriented to small and medium-sized businesses, the agriculture community, and the banking community continue. More than 20 outreach programs were sponsored during the year.

In May of 1985, conferences cosponsored with two accounting firms and the U.S. Department of Agriculture were held in Carmel Valley, California and Chicago. Emphasis was placed on how agribusiness and agriculture cooperatives, in particular, could make use of the ETC Act. Promotion for the conferences was coordinated with major agricultural trade associations. Both conferences were well attended. Subsequent to the conferences, OETCA received an application for a certificate of review from an agricultural export trading company. That certificate has now been issued to California Dried Fruit Export Trading Company.

While Commerce does not administer the Title II banking provisions of the ETC Act, it continues to actively promote use of the Act by the banking community. Two conferences, sponsored by both Commerce and the Treasury Department, were held in San Francisco and New York City. The first was held in February and the second this past October. The purpose of these conferences has been to bring officials from Commerce, Treasury, and the Federal Reserve Board together with representatives of bank ETCs and the banking community in general to share experiences, discuss the benefits available to businesses under the Act, and provide a forum for bank ETC officials to discuss their regulatory concerns. Both conferences were well attended and were conducted on a cost-recovery basis.

In addition to our work with the banking and agricultural communities, OETCA identified Webb-Pomerene Associations and the private antitrust bar as important targets for outreach activities.

The Webb-Pomerene Act of 1918 seeks to provide antitrust protection to export associations. However, in several respects, Webb antitrust protection is inferior to that provided by a Commerce certificate. For example, under the Webb law, export of services is not covered, and their are no provisions for the limited protections from private antitrust suits provided by a Commerce certificate. Moreover, unlike Webb Act associations, Title III certificate holders can engage in importing and domestic commerce, albeit the protection of the certificate only extends to export conduct.

During February-March 1985, 260 letters were mailed to members of Webb-Pomerene Associations that detailed the advantages of a certificate and encouraged Webb members to seek Title III certification.

A major effort was aimed at the members of the antitrust bar. More than eighty letters were mailed to active members of the American Bar Association Antitrust Law Section with details on the ETC Act. A Memorandum of Understanding was entered into between the Department and the Federal Bar Association providing free counseling on the ETC Act to small business clients interested in exporting. OETCA actively supported this cooperative effort and published a manual, entitled Handbook for Professionals, specially designed for lawyers and including a "model" application form. Six hundred fifty copies were distributed nationwide.

Promotion Plans for 1986

Specific promotional activities planned for 1986 include the following:

- **Conduct 9 national ETC Act conferences in cooperation with US&FCS district offices.** Pursuant to an agreement with US&FCS, one ETC conference will be held in each of the 9 regions. The conferences will feature presentations by U.S. exporters that obtained and are using a Title III certificate of review. Promotion of the conferences will include a mass mailing to 55,000 U.S. firms on a combined commercial/SBA mailing list as well as mailings by each of the district offices and notices in Business America, Commerce's magazine. The target audience for these conferences will be small and medium-sized firms.

- **Conduct 2 conferences directed toward public sector utilization of the ETC Act.** OETCA has scheduled, with the National Association of State Development Agencies and the Department's Office of Intergovernmental Affairs, a public sector ETC conference in Washington, D.C. in April 1986. A second conference will be cosponsored with the Saint Lawrence Seaway Development Corporation and will be held in Chicago, Illinois, on September 25, 1986. These conferences will focus on use of the ETC Act by port authorities and local public agencies as well as shippers' associations and small and medium-sized businesses.

- Conduct an ETC Act conference to promote increased use of the ETC Act by agricultural cooperatives. Working with USDA's Agricultural Cooperative Service and Commerce's Office of Business Liaison, OETCA is planning to conduct a one-day workshop on practical applications of the ETC Act for agricultural cooperatives. This conference will be scheduled for late spring or early summer 1986.

- Conduct another bank ETC conference. A bank ETC conference will be scheduled for September 1986. These conferences are part of OETCA's continuing program to encourage the formation of ETCs by eligible financial institutions.

- Special outreach program to encourage use of Title III by shippers' associations. The Shipping Act of 1984 authorized formation of shippers' associations and noted the availability of the antitrust protection of Title III for the concerted action of association members. OETCA has made a special mailing to members of the antitrust bar encouraging them to examine the utilization of Title III for shippers' associations. Two articles for inclusion in shipping publications have been prepared by Commerce staff.

- Work with US&FCS to improve district office ETC outreach activities. OETCA has prepared training materials and ETC counseling guidelines for use by district office personnel. In addition to a detailed explanation of the economic benefits of joint ventures and exclusive dealing arrangements, the materials illustrate the preparation of a Title III application for a certificate of review.

- Continue general ETC Act outreach activities. These include preparation of information for trade association newsletters and export oriented publications as well as presentations at business and trade association meetings.

Contact Facilitation Service

The Department, as part of its responsibility to promote ETCs, has established a Contact Facilitation Service ("CFS") available through any of the Department's 47 District Offices. The CFS is designed to facilitate contact between U.S. producers of goods or services and firms offering export trade services. Companies or individuals who wish to form an ETC may also use the CFS to identify others who are interested in establishing an export trading company.

As originally designed, a CFS user would request a computer search based on identifying characteristics of firms and/or products. In addition to paying a flat fee for the search, the requesting party would also be charged a fee for each name produced by the search. Because this process was significantly underutilized, OETCA elected to format and publish the entire data base in the form of a publication entitled the Contact Facilitation Service Directory. Over 1,700 firms (representing more than 3,000 product lines) appeared in the first edition of the directory published in June 1984. In September 1985, a CFS brochure with a registration form was sent to 55,000 firms throughout the U.S. The second edition of the directory, to be entitled Partners in Export Trade, will provide a listing of more than 4,000 firms with entries from every state. Publication is scheduled for June, and distribution to the public will be through sales by the Government Printing Office. The Department of Commerce will promote sales of the new CFS directory.

Analysis of Promotion Effort

Over the past two fiscal years, OETCA's promotional program has become more targeted to those sectors of the business community that our internal analysis has identified as the most likely beneficiaries of the ETC Act.

It is not possible to identify ETCs that might have been formed directly as a result of OETCA's promotion efforts, but we are aware of many instances in which exporters in those groups targeted by OETCA's Title I programs have subsequently applied for a certificate of review. For example, many of the Federal Reserve Board approved bank ETCs have attended one or more of our bank conferences. We believe that our outreach efforts directed to Webb-Pomerene Associations, shippers' associations, and agribusiness firms have been successful in stimulating utilization of the certificate of review program. Several certificates have been issued to groups of firms belonging to Webb-Pomerene Associations. Two recent applications from shippers' associations are currently being processed. More certificates involving collective export activities have been issued to agribusiness concerns than any other industry group.

It should be noted that the ETC Act contains no requirement that a non-bank ETC identify itself through some form of registration or licensing procedure. Contrary to the impression held by many, the benefits of the Act are available to all exporters, not just ETCs.

Any firm can use the Contact Facilitation Service; any exporter can apply for a Section 206 working capital loan guarantee from the Export-Import Bank; and, any "person" can apply for a Title III certificate of review. Furthermore, the clarification of U.S. antitrust law jurisdiction provided by Title IV extends to all exporters.

Because the original design of the Contact Facilitation Service program called for computer searches of the data base, Commerce would have known how many times the service was used to identify either producers or providers of export services. However, because this service was underutilized, OETCA elected to print the entire data base as a directory and to distribute it in the U.S. and to Commerce and State Department posts overseas. Thus we can not directly monitor usage of the service. The success of our efforts to promote the Contact Facilitation Service is reflected in the significant increase in the number of registrants -- going from 1700 in the first edition to more than 4000 in the forthcoming second edition.

OETCA believes the internal assessment of its Title I programs, together with public feedback, provide a reliable indication about which efforts are the best use of promotional resources. As a part of our internal assessment process, we have used conference evaluations to critique both speakers and subject matter.

TITLE III-- EXPORT TRADE CERTIFICATE OF REVIEW

The Application Process

Commerce encourages each prospective Title III applicant to obtain preapplication counseling from OETCA. These are individualized, confidential meetings to review proposed business plans and to identify what, if any, antitrust considerations they present. Many times the prospective applicant will have a draft that is reviewed at the meeting. In addition to the applicant and its representatives these meetings are attended by a senior member of OETCA's management staff, OETCA's senior antitrust economist, an ETC analyst, and an attorney from the Office of the Assistant General Counsel for Trade Development.

When an application is received by OETCA, it is immediately stamped "received", assigned a number, and reviewed for completeness. This initial review must be completed no later than 5 working days from the date the application was received. If the application is sufficiently complete to be processed, it is date-stamped "Deemed Submitted", and the statutory 90-day processing period starts the next day. If the application is not accepted for processing, the original and all copies are returned to the applicant with a letter describing each deficiency.

Upon acceptance of an application, a copy is sent to the Department of Justice, and OETCA prepares a non-confidential summary of the application for publication in the Federal Register. The summary notice must be delivered to the Federal Register no later than day 10 of the 90-day processing period. Between formal acceptance of an application and day 60, OETCA conducts its research and an economic analysis to determine whether the export conduct for which certification is requested meets the 4 standards of Title III. Should either Commerce or Justice require additional information from the applicant, a request for supplemental information is prepared. The 90-day period is tolled from the date the request is sent until the agencies have received the information and have determined it to be complete.

On or before day 60, Commerce must furnish the Department of Justice a copy of its proposed certificate of review. Justice has until day 80 to either concur or nonconcur with the Commerce draft. If Justice takes no action before the end of day 80, it is deemed to have concurred in issuance of the certificate. In practice, the period between day 60 and day 80, is often marked by discussions between the agencies and the exchange of several redrafts of the proposed certificate.

The Secretary has until the end of day 90 to issue the certificate. If Justice refuses to concur, the applicant has the choice of withdrawing the application or having it denied. Upon issuance of the certificate, a non-confidential summary of the certificate is prepared and delivered for publication in the Federal Register.

Summary of Application Activity Through February 18, 1986

Since June 1983, when OETCA accepted its first application, the office has received 95 Title III applications. Of these 95, applications, 62 have resulted in certificates being issued. Of the remaining 33, 25 were returned for deficiencies, 3 were withdrawn, and 5 are currently in process. Significantly, no application has been denied. Moreover 9 of the applications that were returned for deficiencies were subsequently refiled, assigned a new number, and resulted in certificates being issued. Each of the three withdrawn applications was refiled and in each instance a certificate was issued. The most common deficiency requiring an application to be returned was the failure to adequately describe the export trade activities and methods of operation sought to be certified. In many instances OETCA could not identify an antitrust concern. Another recurring deficiency was the failure to provide financial statements or annual reports. Finally, several applications did not contain sufficient detailed information on products thereby making the requisite economic antitrust analysis impossible to accomplish.

In the case of the 3 applications that were withdrawn, each was at the request of the applicant and involved the submission of a revised application. To date we have issued 5 amendments to previously issued certificates. These amendments were issued at the request of the certificate holders and not as a result of any modification action on the part of Commerce or Justice. There have been no revocation proceedings to date. One holder has voluntarily relinquished its certificate, and one other has indicated an intention to relinquish. Two certificates have expired in accordance with their terms and conditions, and one was vacated by judicial action.

Export Sales by Certificate Holders

As of February 18, 1986, Commerce had issued 43 certificates that were one or more years old, therefore, requiring the filing of one or more annual reports. OETCA actually received 40 reports for the last reporting period. Two holders are late in filing. One has indicated its intention to relinquish the certificate. For their most recent reporting period, aggregate export sales of the 40 reporting firms was $60.2 million. Six of the 40 firms also had export sales in a previous reporting period. These sales for the earlier period totalled $3.5 million. Thus, total export sales reported by certificate holders (exclusive of sales by their members individually) in their annual reports was $63.7 million.

Of the 40 reporting firms, 24 had export sales. Although OETCA has received notice that 2 firms have since terminated their international operations, there is no basis for concluding that the remaining 14 firms, whose annual reports show no export sales, have stopped looking for export trade opportunities or have become operationally dormant. Almost all were start-up operations at the time of their applications. Although the annual reports include information on total domestic sales for the holder during the reporting period, OETCA does not receive information on imports or countertrade transactions.

Employment and Payrolls

A voluntary question in the annual report requests the certificate holder to furnish information on the number of its employees engaged in export trade, and the total payroll for the reporting period attributable to those employees. Of the 40 reports received for the last reporting period, 20 firms specified the number of employees, and 15 of those 20 also furnished the payroll information. In aggregate, the 20 reporting firms employed 262 persons in export activities, and the 15 which provided payroll information showed a combined payroll of $3,021,220 for the reporting period.

Conditions and Restrictions in Certificates

Virtually all certificates have a restriction on the exchange of some types of business information, and a limitation on antitrust protection for export sales financed by the U.S. government. Some certificates also have specific restrictions.

Generic Restrictions

1. Exchange of business information. A general restriction on the exchange of business information is contained in the section of the ertificate captioned "Terms and Conditions of Certificate". The language has varied only slightly among the certificates issued to date. In the case of a certificate covering several firms as "members", the restriction reads as follows:

> "__________ and its Members shall not intentionally disclose, directly or indirectly, to any Member any information about any Member's costs, production, capacity, inventories, domestic prices, domestic sales, domestic orders, terms of domestic marketing or sale, or United States business plans, strategies, or methods that is not already generally available to the trade or public."

In the case where the certificate was issued to a firm that contemplated doing business as an export intermediary for unspecified firms, the first part of the condition would be altered to read:

> "________ will not intentionally disclose, directly or indirectly, to any Supplier any information obtained from a Supplier of the same or similar Products that is about any such Supplier's costs, production capacity, [etc.]."

2. Sales financed by the U.S. government. Initially, the "Disclaimer" section of each certificate contained the following language pertaining to exports financed by the U.S. government:

> "This certificate does not apply to sales to the United States Government or to any sale more than half to cost of which is borne by the United States Government."

In 1985, the Departments of Commerce and Justice agreed to substitute the following language:

> "The application of this certificate to conduct in export trade where the United States Government is the buyer or where the United States Government bears more than half the cost of the transaction is subject to the limitations set forth in Section V. (D) of the 'Guidelines for the Issuance of Export Trade Certificates of Review (Second Edition)', 50 F. R. 1786 (January 11, 1985)."

The Guidelines state that conduct that would otherwise be covered by a certificate, will be covered in the case of U.S. Government financed transactions when either of two conditions is met. First, such conduct is covered where the net effect of any U.S. Government payment or financing involved in an export transaction is not more than half the total cost. Second, even where more than half of the total cost is borne by the U.S. Government, the export conduct will still be covered by the certificate if, because of the nature of the conduct or the existence of substantial competition from unaffiliated persons, the conduct does not substantially reduce competition in the transaction.

Specific Restrictions

In addition to the generic restrictions, some certificates have contained additional specific restrictions. These restrictions fall into the following categories:

1. Market share or other provisions that limit the firms that the certificate holder is protected in dealing with. Such restrictions have been imposed in cases where there would be a substantive antitrust concern if the certificate holder engaged in joint activities with some subset of competitors. This would be the case, for example, if the relevant market was concentrated. We count three instances where such a restriction has been imposed.

2. Specific restrictions on the types of information that can be exchanged, or the methods used in exchanging information. These fall into two categories:

a) Where meetings involving competitors are covered, counsel must be present and accurate written records of such meetings must be maintained. We count three instances in which a certificate contains such a provision.

b) Competitively sensitive information obtained by the certificate holder from suppliers or members can not be revealed to suppliers or members, or can only be reported in a form that does not reveal the identity of the individual firm. (E.g., the data must be aggregated or averaged.) We count five instances in which such a restriction is contained in a certificate.

It should be noted that the restrictions contained in the certificate only affect the protections provided by the certificate. They do not imply that failure to observe the restrictions would be necessarily unlawful. This is specifically pointed out in the section of the certificate captioned "Other Conduct" that reads as follows:

> "Nothing in this certificate prohibits ______ from engaging in conduct not specified in this certificate, but such conduct is subject to the normal application of the antitrust laws."

Annual Reports

Title III of the Export Trading Company requires that certificate holders submit annual reports within 45 days of the anniversary date of their certificates. The annual report forms sent to certificate holders have two parts -- a set of standard questions and, in most cases, a set of specific questions. The latter, referred to as "Appendix A" questions, are tailored to the certificate.

The list of standard questions is divided into two parts. The first part asks for information on domestic and export sales of the certificate holder and members and a copy of the certificate holder's most recent annual financial report. This information is required. The second type of information covered in the standard list of questions concerns employment and payroll related to export operations. This information is voluntary.

The "Appendix A" questions require that the certificate holder provide additional information needed by the Departments of Commerce and Justice for the purpose of monitoring compliance with the standards of the Act. Since the nature of the competitive issues varies from case to case these questions cannot be standardized. In general, more detailed information is asked where the certificate covers activities among firms that are horizontal competitors. (The competitive overlap may be for products not covered by the certificate, however.) As the agencies have gained experience in the certificate program, it has been possible to categorize certificates and introduce a degree of standardization into the Appendix A questions for certificates that do not involve horizontal activities, and, therefore, would normally pose few competitive issues. Such certificates are those for entities intending to do business as pure export intermediaries. In a few cases, no additional information (beyond that asked for the list of standard questions) is requested.

Applicants are advised of the type of annual report questions that will be asked during the latter part of the application process when it is clear precisely what conduct will be covered by the certificate. Before an annual report questionnaire is sent out, the application file is reviewed for any required changes. The questions are then sent to the Department of Justice for comment. A continuing effort is being made to shorten and simplify the annual report questions in order to eliminate any undue burden on certificate holders.

A copy of the current standard questions is given on the next page followed by two copies of Appendix A questions. The first was sent to a certificate holder in a case where the certificate covered a joint export sales arrangement among domestic competitors. The second was sent to a newly establish entity intending to do business solely as an export intermediary.

Summary

The Commerce Department would like to see greater use of the Title III certificate of review program. However, after 2 1/2 years of experience with the Act, OETCA still observes considerable debate among members of the antitrust bar on the level of antitrust certainty provided by a Commerce certificate.

Steps to create even greater certainty in the Title III provisions of the Act may help to clarify the impression of lawyers about the Act. In any event, Commerce has no legislation to propose at this time.

TITLE II--BANK EXPORT SERVICES ACT

It is no secret that the Department of Commerce has expressed its disagreement with certain of the Title II regulations adopted by the Federal Reserve Board. On two occasions -- September 21, 1983 and September 13, 1984 -- Secretary Baldrige wrote the Federal Reserve Board requesting the Board's cooperation in modifying its Title II regulations to provide broader powers to bank ETCs. Basically Commerce views the Board's regulations as too narrow to permit bank ETCs to effectively compete head-to-head with foreign owned ETCs.

As part of its Title I responsibilities, Commerce will continue to encourage the formation of bank ETCs. We will continue to conduct conferences for these trading companies and will continue to solicit the participation of the Federal Reserve Board in these conferences.

CONCLUSION

The Department of Commerce has successfully implemented the Export Trading Company Act. Important precedents have been established, and, as our export environment improves, we can expect to see increased ETC activity.

As the Title III program has matured we have experienced an increasing number of more sophisticated applicants. These involve joint ventures which hold significant potential for realizing scale economies that can provide a competitive edge in the international market place. Such applications also involve substantive antitrust issues as they typically encompass export conduct among domestic competitors. Utilization of the certificate of review program by shippers' associations and to cover technology licensing are areas in which we believe increased activity to be likely.

ANNUAL REPORT QUESTIONS

This form must be signed and dated and returned as part of your submission. Please identify your response by question numbers.

Within 45 days after the anniversary date of the issuance of a certificate of review, you must submit an annual report that updates the information under which the certificate was granted. 50 FR 1804-1812, January 11, 1985 (codified in 15 C.F.R. Section 325.14).

> **THE TERM AND CONDITION IN THE CERTIFICATE CONCERNING THE EXCHANGE OF COMPETITIVELY SENSITIVE INFORMATION APPLIES TO THESE QUESTIONS, PARTICULARLY QUESTIONS TWO AND FOUR. THEREFORE, IT MAY BE NECESSARY FOR EACH MEMBER TO SUBMIT THE REQUIRED INFORMATION SEPARATELY TO AN INDEPENDENT THIRD PARTY, DESIGNATED BY YOU, WHO WILL TRANSMIT THE RESPONSE TO OETCA. PLEASE CONSULT OETCA IF YOU HAVE ANY QUESTIONS CONCERNING THE APPLICABILITY OF THIS CONDITION.**

1. For the combined products and services listed under Export Trade in the the certificate, provide for the certificate holder (in dollars):

   a. the annual domestic sales of the certificate holder;

   b. the annual export sales of the certificate holder.

2. For the combined products and services listed under Export Trade in the certificate, provide for each member separately (in dollars):

   a. each member's annual domestic sales;

   b. each member's annual export sales.

3. If the total sales of products and services exported under the protection of the certificate of review by the certificate holder exceeded $1.0 million, itemize the export sales by product/service lines.

4. Provide the certificate holder's annual financial statement for the most recent fiscal year.

   If the date of the financial statement is more than six months earlier than the certificate anniversary date, also include the most recent quarterly financial statement. Neither annual nor quarterly statements need be audited, but audited statements are preferred if already prepared for the certificate holder.

5. **Specific Questions:**

   a. ________ **None.**

   b. ___X___ **Appendix A, attached.**

   c. ________ **Appendix A as amended, attached.**

6. **Voluntary Information:**

   To help OETCA better assess the effect of the ETC program, we would appreciate the following voluntary information:

   a. **an estimate of the number of employees attributable to your total export activities, and**

   b. **an estimate of the dollar amount of payroll attributable to your total export activities.**

Failure to file an annual report timely could result in the revocation of the certificate of review.

I certify that to the best of my knowledge and belief the information submitted in this report and the attachments is true and correct and fully responds to all annual report questions.

TYPED OR PRINTED NAME	**SIGNATURE (sign in ink)**	**DATE**

APPENDIX A

For each export joint venture proposed or formed by during the reporting year, please provide the following:

(a) The commodity or commodities to be exported or exported by the export joint venture.

(b) The name and principal address of each producer or supplier that solicited to participate in the export joint venture.

(c) The name of each producer or supplier that: (1) responded to solicitation, and (2) if an export joint venture was formed, participated or is participating in the venture.

(d) A copy of the feasibility study, if any, that distributed separately to each of the prospective participants.

(e) A copy of the joint venture agreement entered into by and the producers or suppliers participating in the export joint venture.

(f) The Export Markets to which the joint venture has exported.

(g) For each commodity exported by the joint venture, the dollar volume of the export sales to date.

For each export joint venture formed by prior to the reporting year and which operated during the reporting year, please provide the following:

(h) The export joint venture's operating status.

(i) For each commodity exported by the joint venture, the dollar volume of export sales for the venture's most recent fiscal year.

Appendix A

(1) Provide the name and place of business of each supplier of Products and Related Services with which has entered into an agreement to act as an exclusive distributor or sales representative and the types of Products or Services involved (e.g., wood products, coal, etc.).

(2) Provide the dollar volume of sales of Products and Services handled by for each of the agreements listed under Item (1).

Mr. **Barnard**. Thank you, sir. We will hear from Mr. Dahl.

STATEMENT OF FREDERICK R. DAHL, ASSOCIATE DIRECTOR, DIVISION OF BANKING SUPERVISION AND REGULATION, BOARD OF GOVERNORS, FEDERAL RESERVE SYSTEM

Mr. **Dahl**. Thank you very much, Mr. Chairman, I appreciate very much the opportunity to appear before this subcommittee, on behalf of the Board of the Governors, to discuss the role of the Federal Reserve in implementing the Bank Export Services Act. I shall confine my comments here to some of the highlights in my prepared testimony.

But I would like to say at the outset that I am sure that everyone in this room supports the notion of the furtherance of our export trade. And that includes the Federal Reserve. I think it is fair to say that Chairman Volcker, in testimony before Congress and speeches and other channels, has been tireless in emphasizing the importance of a sound international trade position, including a healthy export trade.

I would like to start with a couple of general remarks on the role of the Board or how the Board envisions itself in implementing the Bank Export Services Act. I think first of all, the Board is charged under the act with carrying out a very difficult balancing act, that is to be consistent with both the letter and spirit of the congressional objective in passage of the legislation of furtherance of our export trade, while at the same time, being attentive to the needs of sound banking organizations.

Because of this balancing act, and because this was landmark legislation insofar as enlarging the role of banking organizations is concerned, the Board has proceeded tentatively, or as one of the other speakers said, in cautious manner. The activities were new, and the effects that they might have on banking organizations were untried. And this, I think, has to do with some of the procedural rules that the Board has put into place which I will revert to later.

Now, that being said, I would like to comment briefly on the experience we have seen under the act, the banking organizations establishing export trading companies, and then go on to focus on some of the criticisms that have been made of the Federal Reserve's role.

Turning to experience we have had in the 3½ years that the legislation has been in place, there have been 40 banking organizations that have notified the Federal Reserve of their intention to establish export trading companies. Most of these notifications were received by early 1985, and in the last year the number of these notifications has declined materially, and the size envisaged for these export trading companies has also diminished. Roughly speaking, before then the average investments were in the range of about $2½ million. Since then the notifications we have received have been on the order of half a million dollars each. But out of these 40 ETC's there are only 29 in an operational mode at the present time. Eleven have withdrawn for various reasons.

But even more significantly among the 29 that are supposedly in an operational mode, it is clear that 7 of those are in rather an idling capacity. And of the remainder, a few are doing trading in goods and commodities, some are concentrating on consulting, a number of others are fundamenally engaged in financing activities of the kind familiar in banks themselves. And finally, all but a few are still incurring operating losses.

Now we have attempted in the Federal Reserve to follow the development of bank ETC's in various ways. But we have not established special reporting requirements on them because of the burden those reports might entail. We have relied instead on some general reports and inspections of bank holding companies which, by their very nature, are discrete and somewhat infrequent. We get some information in the annual reports filed by bank holding companies, but this is limited to just the essence of the financial reports, namely, the balance sheets and something about their income.

As a consequence, the information available to us at all times is not as current as it might be. The reasons for the lack of progress in bank-owned ETC's have been emphasized by other speakers when they have talked about the difficulties of getting started. And more importantly, and more fundamentally about an unfavorable economic environment, both by the economic conditions that are prevalent in the world, and the exchange rate for the dollar. The latter has changed over the last year and that should provide a more conducive environment but it will take some while before we see the results of that.

Now, let me turn, Mr. Chairman, to the criticisms that have been made of the Board's rules and procedures. Most of these are not new. They were discussed in a report we made to the Congress a year and half ago. And they have been repeated by speakers here, and more importantly, in the GAO report. I might say in that regard, that the GAO report that we commented on did not contain the recommendations that appeared approximately 2 weeks ago, and so we have not formally commented on those to the GAO.

Now the first thing about procedures, and here again, I think that I would revert to what I have already mentioned—that the rules that we have followed have been somewhat cautious as we felt our way to seeing what issues might be entailed in the operation of bank-owned export trading companies. This had to do initially with the extent to which notifications had to come to the Board, and in my prepared statement there is reference to the fact that most of these notifications have now been delegated to the Reserve banks, that is for initial establishment. This approach is also reflected in caution about the leveraging involved in export trading companies, and the $2 million inventory rule to which reference has been made by the bank representatives.

I will talk some more later about the leveraging rule. But with a $2 million inventory I would emphasize again that this is not a hard and fast rule of the Federal Reserve. This was an attempt to see or differentiate those companies that were going to engage in taking title to goods, and to looking at their business plans and their intentions.

The Board has indicated, I think, in its response to individual ETC's or banking organizations with the ETC's, that it is prepared to waive that requirement after a review of their business plans.

And this, I would submit, is an indication of the Board's willingness in this trial period, to try to tailor its rules to the circumstances of individual companies.

As to the rules themselves, there have been criticisms of four aspects of them: The revenue test, leveraging, the application of section 23A, and the question of exporting services. Let me deal with them in order.

On the revenues test question, I would emphasize again, that the legislation itself, even its title, has to do with an Export Trading Company Act. It does not have to do with trading companies. It does not have to do with trade. It has to do with export trading companies.

And the 50-percent rule was introduced as an effort to implement that intention of Congress. Indeed, some people have criticized it as being too liberal. As a first approximation the Board has said that companies should have 50 percent of their revenues coming from exports or facilitating exports over a 2-year period. That again, as I indicated, is a first approximation, that is not a hard and fast rule. We have only had a short experience with these companies. We don't know whether this rule is binding or not. It is clearly too early to see whether a much longer period should be used.

Moreover, the Board has indicated that it would be willing in this case, as it has in other cases where it has used a short period of time in the application of certain rules, to consider the circumstances and be prepared to change that as seems appropriate.

The other criticism about the revenues test is the inclusion of such things as third-country trade, and countertrade in the totality of the measurement of the business of the company. I think that the 50-percent rule is consistent with the intention of Congress in this legislation, and the consequences of changing that rule, as has been suggested, to remove all consideration of third-country trade, would be to encourage banking organizations to get into trading opportunities around the world without any assurance that this redounds to the benefit of our export trade, which was the intention of the bill.

And it would certainly be inconsistent with the general notion that has been followed in the United States about banks staying out of trade and commercial trading, especially inside the United States, as being inconsistent with their primary role as provisioners of credit.

The second item is the leveraging question, and the notion of 10 to 1. Again, I submit that this is a screening device by which the Board has asked to look, in this initial period at any rate, at the plans of those companies that propose to have a lower capital ratio in their export trading companies. And as such, anything that the banks intend to do greater than 10 to 1, has to come to the Board for review.

I think it instructive that Mr. Rice from the Chase Trading Co., has just informed you that the Board recently, after a review of their plans and the nature of their business, increased that leveraging condition on the operation of that company to 17 to 1. I believe that the only general principle that the Board has on this issue is that trading companies should at least have the minimum capital requirements established for banks and banking organizations, which is now currently 5½ percent.

I think the Board's position is consistent with the intention of Congress, in the International Lending Supervision Act which mandated the banking agencies to establish firm capital ratios for all banking organizations.

Turning to section 23A the operation of the law is such that it does apply to export trading companies as affiliates of banking organizations. While the Board generally has authority to grant waivers from the provisions of 23A, it has been, as a matter of policy, reluctant to do so.

As noted in my prepared text there has been a general exception granted to export trading companies in relation to their financing of certain trade activities. Apart from that there has been no one else who has applied for a waiver from the provisions of 23A as they affect the operations of their export trading company.

Finally, the Board has been criticized for not allowing export trading companies to engage in any service activities involving transactions with foreigners or outside the United States. The Board believes that this is consistent with the intention of the legislation which was to allow banks to participate in export trading companies that act as intermediaries in promoting exports or the export of services from the United States.

Were this rule to be abolished, it seems to me the consequences would be that it would destroy much of the thrust of the Bank Holding Company Act, which is to maintain both at home and abroad a separation between banking organizations and commercial activity. For example, were it to be abolished they could engage in such services as insurance services, all sorts of——

Mr. **Barnard**. Well, you can name anything.

Mr. **Dahl**. That is the best example I can think of.

Mr. **Barnard**. Well, you have got real estate——

Mr. **Dahl**. Real estate.

Mr. **Barnard** [continuing]. Insurance, investments, merchandising; I mean you name it, you got it.

Mr. **Dahl**. Well, you are way ahead of me, Mr. Chairman, on this, in knowing what they could get up to if this was waived. And we think that is neither consistent with sound banking practices nor with the basic thrust of this legislation.

So in conclusion, I would submit, Mr. Chairman, that we have gone through a very difficult 3½ years in the implementation of this legislation. The environment clearly has not been conducive to the development of these companies nor to the promotion of exports from the United States.

The Board has sought to implement its responsibilities in a flexible fashion, while at the same time being cautious to see what kinds of implications or consequences this might have for sound banking organizations.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Dahl follows:]

For release on delivery
March 4, 1986
11:00 A.M., E.S.T.

Statement by

Frederick R. Dahl

Associate Director

Division of Banking Supervision and Regulation

Board of Governors of the Federal Reserve System

before the

Subcommittee on Commerce, Consumer and Monetary Affairs

of the

Committee on Government Operations

House of Representatives

March 4, 1986

I appreciate the opportunity to appear before this subcommittee on behalf of the Board of Governors to discuss the role of the Federal Reserve in implementing the Bank Export Services Act. The Board has asked me to emphasize that it fully supports both the efforts to assure that the United States has a strong and expanding export sector encompassing a broad range of industries and firms, as well as the specific role that banking organizations, through export trading companies, can play in this effort. Increasing exports is a critical element of a healthy economy. Recognizing this principle, the Board has administered the Bank Export Services Act as Congress intended -- to optimize the usefulness of export trading companies in promoting the export of goods and services from the United States.

As you are aware, the Bank Export Services Act (or BESA), which is Title II of the Export Trading Company Act of 1982, authorizes bank holding companies to acquire equity interests in export trading companies (ETCs), subject to review by the Federal Reserve Board. The BESA was designed to permit banking organizations to participate in promoting the export of U.S. goods and services in a manner consistent with maintaining bank safety and soundness and with avoiding the risks, conflicts and other adverse effects that Congress has sought to prevent through limitations on the combination of banking and commerce. To this end, the BESA requires the Board to review each proposal for potential adverse effects such as unsafe or unsound banking practices, undue concentration of resources, decreased or unfair competition, conflicts of interest, and for a material adverse effect on the safety and soundness of affiliated banks.

Having established these safeguards, Congress permitted these ETCs to engage in a broad range of activities and services that assist in conducting international trade. These include international market research, consulting, insurance, transportation, product research and design, product modification, taking title to goods, and many others.

In October 1984, the Board submitted a report to Congress that described the Board's implementation of the BESA to that date. It is my intention today to provide the subcommittee with an update of that report, including a description of the extent and nature of current operations of ETCs in which banking organizations have invested, and an assessment of their performance. The subcommittee has also asked us to discuss the report prepared by the General Accounting Office (GAO) on ETCs.

The draft report prepared by the GAO, on which the Board commented, was a neutral presentation of issues raised by bank-affiliated ETCs and also discussed the nature and purpose of the Board's regulation of investments by banking organizations in ETCs. Since the Board reviewed the report, the GAO has added one page of policy recommendations, which I will address later in this testimony.

The Board's approach has been to establish regulations that further the chief purpose of the Act -- promotion of exports from the United States -- while maintaining the safety and soundness of the investing banking organizations. I believe that the Board's regulations have met these objectives while keeping its procedures for such investments to a minimum.

Investments by Banking Organizations

At the time of the Board's Report to Congress submitted in October 1984, two years after passage of the Export Trading Company Act, the System had acted upon 29 notifications to establish export trading companies. As of February 28, 1986, the Federal Reserve System had acted upon 40 notifications to make initial investments in export trading companies. As can be seen, most of the activity in investments by banking organizations in ETCs occurred between mid-1983 and early 1985. In the past year, there has been a noticeable decline in such investments. There is currently one notification pending in the Federal Reserve System.

In addition, the System has acted upon eight notices to make additional investments in ETCs or to expand the scope of their activities. The Board has not objected to any notification to establish ETCs or to expand the scope of their activities.

These numbers, however, do not accurately reflect current bank holding company involvement in ETC activity. Eleven of those ETCs on which the Board acted are not currently operational. Accordingly, as of February 28, 1986, there were 29 operating bank holding company-owned ETCs. (Tables attached as an Appendix to this testimony show the status of each ETC notification acted upon by the Federal Reserve System.)

The performance of operating ETCs has been tracked in a number of ways including the annual reports by, and regular inspections of, bank holding companies, and frequent, informal contacts that the Reserve Banks have with bank holding companies in their districts. Drawing on these sources of information, it is clear that the operations of these ETCs have not lived up to expectations. In a number of instances ETCs have scaled back their operations significantly since they opened. All but a few of the active companies have had operating losses.

Many of the difficulties that ETCs have experienced have been those normally associated with the start up of new lines of business. These start-up difficulties have, of course, not been limited to those ETCs owned by banking organizations. In addition to those difficulties, some of the problems that we have seen are peculiar to the activities of trading companies, regardless of how long they have been operating. For example, one ETC encountered substantial difficulties because a major customer broke the terms of its trade agreement; another had its capital wiped out because of its inability to deliver on a major contract; and a third was closed after encountering significant losses because of the holding company's inability to control the trading activities of its ETC. In addition to these cases, at least four bank holding companies have discontinued the operations of their ETCs either temporarily or permanently because the operating losses were found to be unacceptable.

More fundamentally, the fact that ETC performance has not met expectations is attributable to the generally bad export climate that has existed for several years as illustrated by the U.S. trade deficit, which increased from $25 billion in 1980 to an estimated $125 billion in 1985. As is generally well known, the weakness of U.S. exports reflects a number of macroeconomic developments that took place in the early to mid-1980s and that have continued until fairly recently: the very substantial rise of the dollar against foreign currencies; the relatively sluggish growth of real activity in foreign industrial countries; and the drop of imports by countries experiencing debt-burden difficulties, especially Mexico and other Latin American countries.

The appreciation of the dollar until early 1985 has had a particularly severe effect on the international price-competitiveness of U.S. products. A large part of the dollar's appreciation has been reversed over the past several months, but we cannot expect any immediate improvement in U.S. export performance. In fact, increased trade volumes due to the lower dollar are not expected to materialize until well into 1986. Notwithstanding the unfavorable environment for U.S. exports, the normal difficulties of starting new businesses, and bank inexperience with ETCs, a reasonable start has been made in meeting the purpose of Congress to promote U.S. exports. With improved prospects for U.S. export performance and more experience, it is reasonable to expect the outlook for bank-affiliated ETCs to get better.

The factors just mentioned have been the major force delaying development of ETCs affiliated with banking organizations. The Board's administration of the BESA has not been a barrier to accomplishing the goals of the Act. All of the notifications have been acted upon within the 60-day time period set forth in the statute, and no notification by a bank to invest in an ETC has been disapproved. Moreover, in order to expedite review of notifications the Board has decentralized the process and given the Reserve Banks authority to act on most ETC notifications. Fifteen of the 24 notifications to establish ETCs filed after adoption of the delegation procedures were processed by the Reserve Banks with no Board review. In addition, when the Board has reviewed notifications, it has not placed specific limitations or restrictions as a condition of permitting an investment, although it has taken note of, and commented upon, the scope of some of the proposals.

General Accounting Office Report

You have asked the Board to comment on various aspects of the report prepared by the GAO on implementation of the Export Trading Company Act of 1982. I will discuss four issues described in the GAO report on the Board's implementation of Title II of the Act, which I have previously referred to as the BESA. Those issues, which were discussed at length in the Board's 1984 report to Congress on implementation of the BESA, are: (1) the revenues test for ETCs; (2) leveraging of ETCs; (3) exemption of transactions by banks with affiliated ETCs from the requirements of section 23A; and (4) the export of services by ETCs and their affiliated companies.

1. Calculation of Export Revenues

At the outset I must emphasize that the chief purpose of the BESA was the promotion of U.S. exports. The BESA was not designed to promote international trade outside the United States or imports into this country. The BESA defines an ETC as a company that is "exclusively engaged in activities related to international trade" and that is "organized and operated principally for purposes of exporting |or facilitating the export of| goods and services produced in the United States...." This definition reflects Congress' goal of using the facilities and expertise of U.S. banking organizations to improve the export performance of U.S. manufacturing and servicing firms. In accordance with this purpose, the Board's regulations establish that a banking organization may invest in an ETC that derives more than one-half of its revenues over a two-year period from U.S. exports or from facilitating U.S. exports.

This revenues test was designed to ensure that the chief efforts of an ETC are directed to exporting U.S. goods and services, as Congress intended, rather than to trading outside the United States. This position is fully supported by the legislative history of the BESA. The Conference Report states:

> |W|hile it is understood that ETCs will periodically have to engage in importing, barter, third party trade, and related activities, the managers intend that such activity be conducted only to further the purposes of the Act.

According to the GAO report, some bank-affiliated ETCs have advocated excluding from the revenues test those revenues generated from trade outside the United States. They claim that counting those revenues as non-export revenues restricts the ability of ETCs to compete with foreign-owned trading companies. The GAO has also recently revised its draft report to recommend that the Board modify its regulation to exclude from the calculation of export revenues any revenues that come from trade outside the United States.

The reason that the Board has not taken this approach is that it would permit an ETC to engage almost exclusively in trade outside the United States with little or no benefit to U.S. export performance and yet would subject the affiliated U.S. banking organization to all the risks of the trading activity. Such a result is not consistent with Congress' intent in enacting the BESA -- which, as I have stated, permits banking organizations to invest only in ETCs "organized and operated principally for the purpose of exporting goods and services produced in the United States."

2. Leveraging

In reviewing notices by banking organizations to invest in ETCs, the Board considers the assets to equity ratio of each proposed ETC on a case-by-case basis. In this review, the Board takes into account the riskiness of the proposed activities of the ETC. The Board examines carefully the capital structure and proposed leveraging ratios of bank-affiliated ETCs in order to carry out its duty to preserve the safe and sound operation of bank holding companies and their affiliated banks.

In the International Lending Supervision Act, Congress required the bank regulatory agencies to "cause banking institutions to achieve and maintain adequate capital by establishing minimum levels of capital for such banking institutions." In response, bank regulators have moved decisively to improve the capital position of banking organizations. In this process, capital is assessed on a consolidated basis and the capital adequacy of subsidiary organizations must be taken into account. This approach is necessary because the capitalization of affiliated organizations can have an important effect on their related banks.

Capital adequacy is a critical determinant of the financial strength of an ETC and of its ability to withstand unexpected adverse developments. This capital cushion is necessary to prevent an ETC's difficulties from affecting the financial resources of the parent holding company or the safety and soundness of affiliated banks.

In general, the Board is still in the process of assessing the capital needs of ETCs. This process of assessment must remain flexible, and therefore the Board has not established capital, or leveraging, requirements. To the extent ETCs engage in activities posing greater risk, we feel it is not unreasonable to expect ETCs to maintain higher capital ratios than banks. As a general matter, capital levels should be commensurate with the risk of the company's activities.

To streamline ETC notifications, the Board has delegated the authority to review a banking organization's notice of intent to invest in an ETC to the appropriate Federal Reserve Bank. If, however, the proposed leveraging ratio of the ETC exceeds 10:1, then Board review is required. In either case the proposed leveraging ratio and other facts pertaining to the proposal are evaluated on a case-by-case basis.

In this regard, the Board recently received a request from a bank holding company that had established its ETC under the delegated procedures. The bank holding company sought to adopt a leveraging ratio for its ETC that was higher than the 10:1 ratio it had proposed to the Reserve Bank earlier. After evaluating the nature and riskiness of the activities proposed for the ETC, the Board approved a leveraging ratio of 17:1. The Board has not conditioned approval of any ETC notice on a specific leveraging ratio.

3. Exemption of Transactions by Banks with Affiliated ETCs from the Requirements of Section 23A

The BESA provides that transactions between a bank and its affiliated ETC are covered by section 23A of the Federal Reserve Act. Section 23A generally limits the amount of credit that banks may extend to a nonbank affiliate and subjects such credit extensions to certain collateral requirements. The purpose of Section 23A is to protect the safety and soundness of the bank on a general basis by identifying and restricting those classes of affiliate transactions that could result in losses to a bank because the affiliate relationship may have colored the bank's objectivity in evaluating the credit worthiness of the borrower.

Experience over the years has demonstrated that limitations on self-dealing between a bank and its affiliates are essential to prevent abuses, to maintain bank safety and soundness and to prevent excessive risk to the federal safety net. Accordingly, the Board as a matter of policy has generally not granted exemptions from section 23A. With respect to ETCs, however, the Board has nevertheless included in its regulations a waiver from the strict collateralization standards of section 23A for those transactions in which the ETC takes title to goods against a firm order and the lending bank maintains a security interest in those goods. The Board has determined that a waiver from section 23A in these circumstances would permit ETCs to obtain financing for transactions in goods without creating undue risk to the affiliated bank. In addition, the Board has stated that it would consider granting ETCs additional waivers from the collateral requirements of section 23A based on specific requests.

The experience to date, though limited, reinforces the desirability of maintaining the protections afforded by section 23A. In at least one instance that we are aware of, a bank lent to its affiliated ETC in violation of section 23A. The loan went bad because of misjudgments on the trading side, and significantly affected the condition of the bank. Therefore, we question the wisdom of a total exemption from section 23A for transactions with an ETC, as some bank-affiliated ETCs are reported by the GAO to have suggested. Especially in the area of extensions of credit, it is important to strike the balance between encouraging the growth of ETCs and preventing imprudent banking practices.

4. Exporting Services

The BESA requires that a bank-affiliated ETC engage "exclusively" in activities related to international trade and "principally" in exporting or facilitating exports from the United States. Congress permitted an exception to the traditional separation between banking and commerce for investments by banking organizations in ETCs because it viewed banks as "the best intermediary between the potential U.S. exporter and the foreign buyer because they already have offices (branches) at both ends of the chain, and are already communicating with business people on both ends." To further this purpose, the Board's regulations provide that an ETC in which a banking organization may invest must derive more than one-half its revenues from exporting or facilitating the export of goods and services produced in the United States by persons other than the ETC or its subsidiary.

Under the BESA and the Board's regulations, a banking organization may invest in a company that offers any of a variety of services that in one way or another facilitate trade. A banking organization, however, may not invest in any company of its choice simply because that company has foreign customers. Such an interpretation would have the effect of substantially increasing the scope of activities in which a bank holding company could engage both in the United States and abroad. It not only would deviate from the purpose of the BESA but would disrupt the framework that Congress has established in the Bank Holding Company Act for investments by bank holding companies in other nonbanking companies. It would permit banking organizations to invest in an ETC engaged in an otherwise prohibited nonbanking activity simply on the grounds that the company had foreign customers.

The Board's regulations do not limit the ability of bank-affiliated ETCs to provide trade services. On the contrary, the BESA and the Board's regulations permit bank-affiliated ETCs to offer a broad range of trade-related services both in the United States and abroad. For example, the BESA and the regulations permit ETCs to provide consulting, market research, marketing, insurance, product research and design, legal assistance, transportation including freight forwarding, warehousing, foreign exchange, financing and taking title to goods, when provided in order to facilitate the trade in goods and services produced by others. According to the notifications to the Federal Reserve, a number of ETCs are providing many of the trade services listed in the statute. Moreover, the Board has recognized that this list of services is not exhaustive. As an example, upon demonstrating that the activities were related to international trade, one ETC has acquired a company in England that engages in customs bonding services and in certain types of inventory control services related to cross-border trade.

A bank-affiliated ETC may provide these and other trade services to any of its affiliates (other than a subsidiary), including its parent bank holding company and its bank and nonbank affiliates, and to its customers in order to facilitate the export from the United States of the services of the affiliate or the customer. Revenues derived from such services would be considered export revenues under the Board's regulations. A bank-affiliated ETC could also form a joint venture with a manufacturing or a service company in order to export the goods or services of the joint venture partner. Revenues derived from these activities are also considered export-related and count toward meeting the revenues test in the Board's regulations.

Summary

In sum, we believe that the Board's regulations appropriately implement the BESA by furthering the purpose of the statute to promote the export of U.S. goods and services while maintaining the safety and soundness of the banking organizations that invest in ETCs. The Board has sought to maintain flexibility in its approach to such investments because of the difficult export environment and because there is still little experience with the industry generally. The Board expects to continue to review its policies in light of increased experience regulating investments in ETCs and in response to individual requests.

APPENDIX

NOTIFICATIONS TO ESTABLISH EXPORT TRADING COMPANIES

Bank Holding Company	Export Trading Company	Date of System Action	Current Status
Security Pacific Corporation, San Francisco, CA	Security Pacific Export Trading Company Los Angeles, CA	5/09/83	Operating
Citicorp, New York, NY	Citicorp International Trading Company, New York, NY	5/31/83	Operating
Walter E. Heller International Corporation, Chicago, IL	Heller Trading Company Chicago, IL	6/13/83	Closed
First Interstate Bancorp, Los Angeles, CA	First Interstate Trading Company, Los Angeles, CA	6/15/83	Operating
First Kentucky National Corporation, Louiseville, KY	First Kentucky National Trading Company, Louiseville, KY	7/25/83	Inactive
Union Bancorp, Inc., Los Angeles, CA	StanChart Export Services Company, Inc., Los Angeles, CA	7/25/83	Operating
Crocker National Corporation, San Francisco, CA	Crocker Pacific Trade Corporation, San Francisco, CA	8/30/83	Closed
Ramapo Financial Corp., Wayne, NJ; Ultra Bancorporation, Bridgewater, NJ; and New Jersey National Corporation, Trenton, NJ	Bancorp's International Trading Corporation, Somerset, NJ	9/14/83	Operating
State Street Boston Corporation, Boston, MA	State Street Trade Development Corporation, Inc., Boston, MA	9/19/83	Sold

Bank Holding Company	Export Trading Company	Date of System Action	Current Status
International Bancshares Corporation, Laredo, TX	IBC Trading Company, Laredo, TX	10/03/83	Not Activated
United Midwest Bancshares, Inc., Cincinnati, OH	United Midwest International Corporation, Cincinnati, OH		Closed
U.S. Bancorp, Portland, OR	U.S. World Trade Corporation, Portland, OR	11/17/83	Inactive
First Chicago Corporation, Chicago, IL	First Chicago Trading Company, Chicago, IL	11/21/83	Operating
Rainier Bancorporation, Seattle, WA	Rainier International Trading Company, Seattle, WA	12/07/83	Operating
Shawmut Corp., Boston, MA	Shawmut Export Corporation, Boston, MA	12/12/83	Operating
Hongkong and Shanghai Banking Corporation, Hong Kong	Equator Trading Company Limited, Hartford, CT	12/27/83	Operating
BankAmerica Corporation, San Francisco, CA	BankAmerica World Trade Corporation, San Francisco, CA	02/02/84	Inactive
Bankers Trust New York Corporation, New York, NY	Bankers Trust International Trading Corporation New York, NY	02/02/84	Operating
First National State Bancorporation, Newark, NJ	First International Trading Co., Newark, NJ	02/13/84*	Operating
Chase Manhattan Corp., New York, NY	Chase Trade, Inc., New York, NY	02/21/84*	Operating
Society Corporation, Cleveland, OH	Export Partnership for International Trade, Inc., Cleveland, OH	03/04/84	Operating
Fleet Financial Group, Inc. Providence, RI	Fleet Trading Company, Providence, RI	03/19/84*	Inactive
First National Bancshares, Inc. Houma, LA	First Export Corporation, Houma, LA	04/06/84*	Operating

*Acted upon by Reserve Banks pursuant to Delegated Authority.

Bank Holding Company	Export Trading Company	Date of System Action	Current Status
Manufacturers Hanover Corporation, New York, NY	C.I.T. International Sales Corporation, New York, NY	04/24/84	Operating
First Union Corporation, Charlotte, NC	First Union Export Trading Company, Charlotte, NC	05/07/84*	Operating
Alaska Mutual Bancorporation, Anchorage, AK	Mutual International Corporation, Anchorage, AK	06/06/84*	Operating
Frontier Bancorp, Vista, CA	Interbank Trading Company, San Diego, CA	07/30/84*	Not Activated
Florida Park Banks, Inc. St. Petersburg, FL	Park Services International, Inc., St. Petersburg, FL	09/19/84	Closed
Capital Bancorp, Miami, FL	Capital Trade Services, Inc., Miami, FL	09/20/84*	Operating
CoreStates Financial Lancaster, PA	CoreStates Export Trading Company, Philadelphia, PA	10/13/84*	Operating
North Valley Bancorp, Redding, CA	North Valley Trading Company, Redding, CA	10/18/84*	Operating
Maryland National Corporation, Baltimore, MD	MN Trade Corporation, Baltimore, MD	12/18/84*	Operating
Marine Corporation, Milwaukee, WI	Marine Financial Services, Inc., Milwaukee, WI	12/31/84*	Operating
Ramapo Financial Corp., Wayne, NJ; Ultra Bancorporation, Bridgewater, NJ; and New Jersey National Corporation, Trenton, NJ	Florida Interbank Trading Company, Inc., Jacksonville, FL	01/07/85	Operating
First Wisconsin Corp., Milwaukee, WI	InterContinental Trading Co., Inc., Rolling Meadows, IL	02/11/85	Operating

*Acted upon by Reserve Banks pursuant to Delegated Authority.

Bank Holding Company	Export Trading Company	Date of System Action	Current Status
Commerce Union Corporation, Nashville, TN	Commerce Trading Corporation, Nashville, TN	03/22/85	Operating
Valley National Corporation, Phoenix, AZ	Valley International Trading Company, Phoenix, AZ	04/16/85*	Operating
Manufacturers Hanover Corporation, New York, NY	Manufacturers Hanover World Trade Corporation, New York, NY	04/21/85*	Operating
Marine Midland Banks, Inc., Buffalo, NY	Marine Midland Trade, Inc., New York, NY	04/21/85*	Operating
United Bancorp of Arizona, Phoenix, AZ	United Bank Export Trading Company, Phoenix, AZ	07/05/85	Operating
InterFirst Corporation, Dallas, Texas	InterFirst World Trade Corporation, Dallas, Texas	—	Pending

*Acted upon by Reserve Banks pursuant to Delegated Authority.

OTHER EXPORT TRADING COMPANY NOTIFICATIONS

Bank Holding Company	Export Trading Company	Date of Notice	Date of System Action[1]	Request
Security Pacific Corporation, Los Angeles, CA	Security Pacific Trading Co.	11/21/83	01/18/84	Expand Activities[2]
Society Corporation, Cleveland, OH	Export Partnership for Intercontinental Trade Inc.	01/23/85	03/20/85	Additional Investment
Hongkong and Shanghai Banking Corporation, Hong Kong	Equator Trading Co.	02/06/85	04/05/85	Additional Investment
Citicorp, New York, NY	Citicorp International Trading Co.	03/19/85	04/09/85	Additional Investment
State Street Boston Corp., Boston, MA	State Street Trade Development Co., Inc.	06/07/85	07/29/85	Additional Investment
Citicorp, New York, NY	Citicorp International Trading Co.	09/10/85	11/06/85	Invest in Bonded Collateral Management Vehicle
State Street Boston Corp., Boston, MA	State Street Trade Development Co., Inc.	10/31/85	12/19/85	Additional Investment
Chase Manhattan Corp., New York, NY	Chase Trade, Inc.	11/04/85	02/26/86	Increase Leveraging[3] to 17:1

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[1] In each instance, the Federal Reserve had no objection to the proposal.

[2] In its notification to the Board to establish its ETC, Security Pacific sought to engage in only limited ETC activities. The purpose of this notification was to enable it to engage in the full scope of the activities permitted under the BESA.

[3] Technically, this request was for relief from a commitment, not an ETC notification.

Mr. **Barnard**. Thank you, Mr. Dahl.

I am going to pose some questions to Mr. Lacy first, and then I will pose some questions to Mr. Dahl.

Mr. Lacy, your annual reports from ETC's show that of 40 reporting firms, 24 had export sales; 2 had terminated their operations; and the remaining 14 firms did not show export sales. Has the Department of Commerce conducted any surveys, or made any inquiries of these 14 firms to determine why they have not shown any export sales?

Mr. **Lacy**. No; we haven't. The annual reports are used for the Commerce Department and the Justice Department to be able to make a continuing analysis of the antitrust issues that are the feature of the certificate of review. We know that for the reporting period that those 14 participants in certificates did not report export activity. I might note that this does not mean that those organizations have not been seeking opportunities to export, or will not be exporting in the future.

Mr. **Barnard**. Mr. Lacy, do directors of the Export Company Affairs—is that your exclusive function in the Department of Commerce?

Mr. **Lacy**. Yes.

Mr. **Barnard**. In promoting the formation of export trading companies?

Mr. **Lacy**. And administering the Title III Certificate of Review Program.

Mr. **Barnard**. Do you have a mechanism whereby you can measure the response, the success, of your promotions?

Mr. **Lacy**. No; we can't. And we stated that in our prepared testimony. The fact of the matter is that as far as export trading companies are concerned, only those export trading companies that either are bank affiliated, or apply for a certificate of review at the Commerce Department need register with the Government.

So the only universe that we have for determining those that have, in fact, formed are those two certification or application processes. We don't have a device for monitoring nonbank export trading companies that do not have antitrust concern, for example, because they are not covered by any other filing programs with the Government.

Mr. **Barnard**. So you cannot really track what Mr. Chew has talked about, and that is the export management companies?

Mr. **Lacy**. We track the export management companies by working with associations like Mr. Chew's assocation, the National Federation of Export Associations, for example. We have been very involved in working in cooperative programs, with trade associations that represent export trading companies. And then there is the Council for Export Trading Companies.

So we take seriously the responsibility to promote export trading companies. But we have no way of determining what numbers have been established since the passage of the act.

Mr. **Barnard**. Mr. Lacy, does your division utilize any of the information that is developed from Commerce's Foreign Commercial Service, or the Domestic Commercial Service?

Mr. **Lacy**. Yes; in the past we have conducted mailings to certificate holders which have included trade-lead information through the U.S. and FCS TOPS trade-lead program. We have also done mailings to holders of certificates as well, that have included copies of Business America, which is the trade development magazine of the Commerce Department. Our cooperative efforts with the U.S. and Foreign Commercial Service include these nine national ETC conferences that I mentioned earlier. I might add that I have a 17-member staff; however, export trading companies are a departmental priority at the Commerce Department.

My office isn't the only center of activity to support export trading company development. We have organized this year cooperative efforts with, for example, Secretary Baldrige's Office of Business Liaison, the Office of Intergovernmental Affairs, and the Office of General Counsel plays a supportive role in our promotion activities. From a governmental standpoint, last year we organized three conferences that were cosponsored with the Department of Agriculture, oriented specifically toward that sector. And the Department of Treasury has cosponsored four conferences with us for the banking industry as well as having participation by the Federal Reserve Board.

Mr. BARNARD. Mr. Lacy, have you studied the bill, the new legislation proposed by Senator Heinz?

Mr. LACY. I have read the bill.

Mr. BARNARD. Has the Department of Commerce reached an opinion on the legislation?

Mr. LACY. Commerce and the administration have not arrived at an opinion on the legislation. I might point out that in Under Secretary Smarts' response to receipt of the GAO report, he specifically welcomed the discussion of the title II issues in the report. And I feel it's fair to say that the members of the Department of Commerce here are encouraged by the discussion at this hearing on that issue. Several of the points touched on in the legislation deal with issues that Secretary Baldrige has raised with Chairman Volcker in exchanges of correspondence. [See app. 4.]

But beyond that I have to say that the administration does not have an opinion on the legislation.

Mr. BARNARD. Are you familiar with the seven points that were introduced in Mr. Chew's testimony today, that would enhance the act as far as export nonbank trading companies; are you familiar with those?

Mr. LACY. I have read the article. It has been a few months. I remember one of the points specifically because it deals with our office at the Commerce Department.

One of his proposals is to put antiboycott compliance in our office at the Commerce Department. We come unprepared to make a statement on whether or not we would support or oppose such legislation. We would have to look at it at 14th and Constitution.

[SUBCOMMITTEE NOTE.—This is the location of the Department of Commerce.]

Mr. BARNARD. Thank you very much.

[SUBCOMMITTEE NOTE.—The subcommittee requested and the Commerce Department provided the following information:]

UNITED STATES DEPARTMENT OF COMMERCE
International Trade Administration
Washington, D.C. 20230

April 28, 1986

RECEIVED
MAY 2 1986
COMMERCE, CONSUMER AND
MONETARY AFFAIRS SUBCOMMITTEE

Honorable Doug Barnard, Jr., Chairman
Commerce, Consumer, and Monetary
  Affairs Subcommittee
Committee on Government Operations
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

Thank you for your letter of March 21. I appreciate the opportunity to augment my testimony of March 4 by responding to the questions and providing the information requested in your letter.

I respectfully request the enclosed answers to your questions be submitted for the record and included in the published record of hearings on the Export Trading Company Act of 1982.

If I can be of further assistance, please let me know.

Sincerely,

James V. Lacy, Director
Office of Export Trading Company Affairs

Enclosures

QUESTION:

In addition to the extensive export trading company promotion efforts by your office, please specify and describe any efforts to provide management, financial, or trade-related counseling to ETCs once they have been established (irrespective of whether or not they are "certified" for antitrust protection).

ANSWER:

Since its inception the Office of Export Trading Company Affairs (OETCA) has conducted several hundred counseling sessions with firms and individuals seeking information about the Export Trading Company Act or answers to other questions regarding international trade. In many instances the party being counseled was an existing firm examining ways to enter foreign trade or to become more competitive in overseas markets. Almost all of our counseling sessions include a discussion of business arrangements for which Title III antitrust protection might be desirable. Because this discussion necessarily involves the firm's business plans, a counseling session typically covers a wide range of business considerations. Some of the more common topics include the desirability of exclusive supplier or distributorship contracts; joint export ventures with domestic competitors; creation of a shippers' association; antitrust protection for contractual restraints included in technology licensing; trade finance and financial assistance programs; and the requirements for, and tax benefits of, a Foreign Sales Corporation.

In addition to the individualized confidential counseling sessions, OETCA provides information and advice on these and related topics at the ETC conferences conducted throughout the U.S. that are attended by both existing exporters and firms that are new to exporting. For your convenience, I have enclosed copies of some conference agenda which illustrate the range of topics covered. I have also enclosed a copy of the flier announcing the dates and locations of the current round of ETC Act conferences OETCA is conducting with US&FCS District Offices.

Distribution of our Export Trading Company Guidebook is another way OETCA provides management, financial and trade related counseling to established firms. The Guidebook covers all aspects of the ETC Act and includes models of ETCs with *pro forma* financial statements extending through the first four years of operation.

Finally, we encourage all existing firms that either produce exportable goods or services or provide trade facilitation services to take advantage of OETCA's Contact Facilitation Service (CFS) by registering, without cost, through their nearest Commerce District Office. In 1984, the first CFS Directory was published with a listing of about 2,000 firms. In September 1985 a CFS brochure with a detachable registration form was sent to 55,000 firms throughout the U.S. This mailing significantly improved the number of CFS registrants. A second edition of the Directory containing the names of close to 5,000 firms will be published this summer.

QUESTION:

You indicated on page 21 of your written statement that there is still considerable debate among members of the antitrust bar on the level of antitrust protection provided under the Act and that "steps to create even greater certainty in the Title III provisions of the Act may help clarify" the situation.

a. Please describe this ambiguity and uncertainty, particularly among members of the antitrust bar?

b. In your judgment, what changes would you suggest to clarify this situation?

ANSWER:

Some of the uncertainties surrounding Title III have been underscored by recent litigation involving a certificate of review. The principal issue highlighted by the litigation is the scope of review of the Secretary's determination to issue a certificate. In addition members of the private bar have expressed concern that the third certification standard can be construed to create a new private cause of action.

We do not suggest changes to Title III at this time. We will continue the manner in which we have implemented Title III. We plan to continue to monitor Title III to determine whether any statutory changes may be desirable.

QUESTION:

Please furnish us all correspondence between the Commerce Department's Industry Sector Advisory Committee and (a) Commerce Secretary Baldrige, and (b) the U.S. Trade Representative, concerning the Export Trading Company Act's implementation, including concerns about the Federal Reserve Board's ETC regulations?

ANSWER

In response to the third item of your letter, we are enclosing copies of the correspondence between the Department's Industry Sector Advisory Committee and (a) Secretary Baldrige, and (b) the U.S. Trade Representative, concerning Title II of the ETC Act and the Federal Reserve Board's regulations.

Honorable Malcolm Baldrige
Secretary of Commerce
Washington, D.C. 20230

Dear Mr. Secretary,

The Industry Sector Advisory Committee for Services (ISAC-13) has reviewed the regulations of the Federal Reserve Board (FRB) (12 CFR Part 211, Subpart (C) concerning bank-affiliated export trading companies. We believe that the regulations are inconsistent with the statute (Title II of the Export Trading Company Act of 1982), and that the regulations have hindered the successful development of bank-affiliated ETCs. The clear legislative mandate of Congress to the FRB was to encourage and assist in the growth of ETCs. We believe that FRB has ignored its directive to pursue regulatory policies that "provide for the establishment of export trading companies with powers sufficiently broad to enable them to compete with similar foreign-owned institutions in the United States and abroad." (Section 202(1) of the Export Trading Company Act of 1982). Instead the FRB has presented major obstacles to the ETC concept. The following are some of the specific regulatory and policy positions that have hindered the growth of bank-affiliated ETCs:

1. The FRB regulations generally limit to ~~$2 mill~~ion the value of goods which the ETC can take title without a firm order for resale (Final Rule, December 27, 1983, 48 Fed. Reg. 56938). This artificial and arbitrary limit reduces the ETC's trading flexibility and substitutes the FRB's judgment on appropriate inventory levels for the more experienced judgment of ETC management. In practice ETCs can be expected to operate prudently with respect to inventory policy. If the FRB determines that a specific ETC's inventory policies pose a treat to the safety and soundness of the affiliated bank, it might then be reasonable to limit that ETC's operations. But a $2 million limit for all ETCs is arbitrary and not required by the statute.

2. The FRB regulations generally limit a bank-affiliated ETC to debt-to-capital ratio of not more than ~~10 to 1~~. (Final Rule, December 27, 1983, 48 Fed. Reg. 56938). This arbitrary figure bears no relation to the leverage customary with trading companies not affiliated with banks. Foreign trading companies frequently have ratios in excess of 20 to 1. Again, if the FRB believed that if a specific ETC's leverage had an adverse impact on an affiliated bank, the FRB could limit that ETC's leverage. As with inventory, the FRB has arbitrarily substituted its judgment for the more informed judgment of ETC management on the proper leverage needed to make the ETC competitive and profitable.

3. Application of Section 23A. In direct conflict with the intent of Congress, the FRB is imposing collateral requirements and other conditions on the borrowings of ETCs from affiliated banks. A major premise behind allowing bank holding companies to invest in export trading companies was to utilize the bank's financial resources and know-how to stimulate export transactions. The collateral requirements severely limit the ability of a bank to bring its full financial resources to the assistance of the ETC. The FRB should substantially broaden the limited exemption from the collateral requirements in 12 CFR 211.33(b)(3).

4. Counting revenue under the 50 percent rule. The FRB regulations require a bank-affiliated ETC to derive more than 50 percent of its revenue from U.S. exports or from the facilitation of U.S. exports in any two-year period (12 CFR 211.32(a). This requirement is not in itself unreasonable. However, the manner in which revenue is counted as U.S. export-related fails to accord with the reality of current international trade practices. Countertrade arrangements have grown increasingly important in the conduct of international trade and often provide the only mechanism whereby a U.S. exporter can gain access to many overseas markets. For example, assume that a bank-affiliated ETC facilitates the export of a U.S. product, takes goods in countertrade as payment, and earns a fee for the entire transaction. Although the FRB regulations are unclear, it appears that the fee would have to be allocated between the export part of the transaction and the countertrade part of the transaction. An allocation of more than hold the fee to the countertrade part would actually hinder the ETC from meeting the 50 percent revenue test, even though the countertrade allowed an export transaction to go forward which otherwise might not have occurred at all. The entire fee in such a transaction should be considered as export-related revenue. At the very least, the FRB should not penalize the ETC by a negative treatment of the countertrade part of the transaction.

5. Export of services. In a manner completely unsupported by the statute or the legislative history, the FRB regulations prohibit a bank-affiliated ETC from exporting its own services (12 CFR 211.32(a)). Congress clearly intended to empower bank-affiliated ETC's to export goods and services or facilitate the export of goods and services. Congress did not want bank-affiliated ETCs to engage in manufacturing or in agriculture, and said so clearly in the statute. But it had no intent to limit the services offered by bank-affiliated ETCs. Bank-affiliated ETCs possess distinct comparative advantages in dealing in services, and trade in services is as important to our future balance of trade position as trade in goods. Although you have called this matter to Chairman Volcker's

attention, the FRB's response to your letters has not been adequate. In essence the FRB requires a bank-affiliated ETC to enter into a joint venture with an unaffiliated service company in order to export services. The joint venture often proves a very difficult and inefficient way to conduct international trade. The affect again is to reduce the effectiveness of ETCs, not encourage or promote them.

ISAC-13 submits that the FRB should amend its regulations to reduce these regulatory burdens on bank-affiliated ETCs. Instead of placing obstacles in the path of this new industry the FRB should be doing more to encourage ETC development. We will support whatever action you can take to foster such amendment

Sincerely,

Peter Finnerty

JAN 21 1986

Mr. Peter J. Finnerty
Chairman, ISAC-13
Sea-Land Corporation
P.O. Box 800
Iselin, New Jersey 08830

Dear Mr. Finnerty:

Thank you for your letter providing ISAC-13's recommendations for changes in the Federal Reserve Board regulations on bank-affiliated export trading companies (ETC's). I will urge Chairman Volcker and the Board to give them serious consideration. Also, the Export Trading Company Amendments Act of 1985, introduced by Senator Heinz on December 12, 1985, addresses each of the five changes recommended by ISAC-13.

Since the ETC program began, the Commerce and Treasury Departments have conducted three bank ETC conferences to provide a forum for the exchange of views between the banking industry and Federal officials who administer the ETC Act. At our most recent conference in New York City on October 3, 1985, each of the issues addressed by ISAC-13 was identified as a factor inhibiting the operations of bank-affiliated ETC's.

Another forum for discussing improvement of the Board's regulations will be at hearings planned by the Subcommittee on International Finance and Monetary Policy of the Senate Committee on Banking, Housing and Urban Affairs. Although the date for these hearings has not been set yet, I expect that interested representatives from the private sector will have an opportunity to voice their objections to the way the Board regulates bank-affiliated ETC's and to give their views on the amendments proposed by Senator Heinz.

We look forward to working with you in encouraging the formation and success of ETC's.

Sincerely,

alcolm Baldrige

Secretary of Commerce

Drafted By: Prepared by:
ID #1025 LIB. DUCUCS Control #OS524318 & OS524294
cc:ES(2),SEC,HR,D/S,OCA,GC,PC,CHRN,AS/TD,AGC,Farren
1/07/86

Sea-Land Corporation

524294

Peter J. Finnerty
Vice President
Public Affairs

INDUSTRY SECTOR ADVISORY COMMITTEE
FOR TRADE POLICY ON SERVICE INDUSTRIES

(ISAC-13)

December 20, 1985

Honorable Clayton P. Yeutter
United States Trade Representative
600 17th Street, N.W.
Washington, D. C. 20506

Dear Ambassador Yeutter,

The Industry Sector Advisory Committee for Services (ISAC-13) has reviewed the regulations of the Federal Reserve Board (FRB) (12 CFR Part 211, Subpart (c) concerning bank-affiliated export trading companies. We believe that the regulations are inconsistent with the statute (Title II of the Export Trading Company Act of 1982), and that the regulations have hindered the successful development of bank-affiliated ETCs. The clear legislative mandate of Congress to the FRB was to encourage and assist in the growth of ETCs. We believe that FRB has ignored its directive to pursue regulatory policies that "provide for the establishment of export trading companies with powers sufficiently broad to enable them to compete with similar foreign-owned institutions in the United States and abroad." (Section 202(1) of the Export Trading Company Act of 1982.) Instead the FRB has presented major obstacles to the ETC concept. The following are some of the specific regulatory and policy positions that have hindered the growth of bank-affiliated ETCs:

P.O. Box 800 Iselin, New Jersey 08830 Tel: (201) 632-2241

1. The FRB generally limits to $2 million the value of goods which the ETC can take title without a firm order for resale (Final Rule, December 27, 1983, 48 Fed. Reg. 56938). This artificial and arbitrary limit reduces the ETC's trading flexibility and substitutes the FRB's judgment on appropriate inventory levels for the more experienced judgment of ETC management. In practice ETCs can be expected to operate prudently with respect to inventory policy. If the FRB determines that a specific ETC's inventory policies pose a threat to the safety and soundness of the affiliated bank, it might then be reasonable to limit that ETC's operations. But a $2 million limit for all ETCs is arbitrary and not required by the statute. The statute does have prudential limits on the amount of capital and financing that a bank holding company or affiliated bank can make available to an ETC. In addition, the FRB has the authority to examine ETCs. We believe that these prudential limits and the examination authority provide the FRB with sufficient means to ensure the safety and soundness of the affiliated banks.

2. The FRB generally limits a bank-affiliated ETC to debt-to-capital ratio of not more than 10 to 1. (Final Rule, December 27, 1983, 48 Fed. Reg. 56938.) This arbitrary figure bears no relation to the leverage customary with trading companies not affiliated with banks. Foreign trading companies frequently have ratios in excess of 20 to 1. Again, if the FRB believed that if a specific ETC's leverage had an adverse impact on an affiliated bank, the FRB could limit that ETC's leverage. As with inventory, the FRB has arbitrarily substituted its judgment for the more informed judgment of ETC management on the proper leverage needed to make the ETC competitive and profitable. As indicated above, the statute does provide prudential limits and the FRB has examination authority.

3. Application of Section 23A. In direct conflict with the intent of Congress, the FRB is imposing collateral requirements and other conditions on the borrowings of ETCs from affiliated banks. A major premise behind allowing bank holding companies to invest in export trading companies was to utilize the bank's financial resources and know-how to stimulate export transactions. The collateral requirements severely limit the ability of a bank to bring its full financial resources to the assistance of the ETC. The FRB should substantially broaden the limited exemption from the collateral requirements in 12 CFR 211.33(b)(3) or support a total exemption from Section 23A.

4. Counting revenue under the 50 percent rule. The FRB regulations require a bank-affiliated ETC to derive more than 50 percent of its revenue from U.S. exports or from the facilitation of U.S. exports in any two-year period (12 CFR 211.32(a). This requirement is not in itself unreasonable. However, the manner in which revenue is counted as U.S. export-related fails to accord with the reality of current international trade practices. Countertrade arrangements have grown increasingly important in the conduct of international trade and often provide the only mechanism whereby a U.S. exporter can gain access to many overseas markets. For example, assume that a bank-affiliated ETC facilitates the export of a U.S. product, takes goods in countertrade as payment, and earns a fee for the entire transaction. Although the FRB regulations are unclear, it appears that the fee would have to be allocated between the export part of the transaction and the countertrade part of the transaction. An allocation of more than half the fee to the countertrade part would actually hinder the ETC from meeting the 50 percent revenue test, even though the countertrade allowed an export transaction to go forward which otherwise might not have occurred at all. The entire fee in such a transaction should be considered as export-related revenue. At the very least, the FRB should not penalize the ETC by a negative treatment of the countertrade part of the transaction. We recommend that the FRB adopt a rule that only requires U.S. export revenue to exceed U.S. import revenue.

Honorable Clayton P. Yeutter
Page Four
December 20, 1985

5. Export of services. In a manner completely unsupported by the statute or the legislative history, the FRB regulations prohibit a bank-affiliated ETC from exporting its own services (12 CFR 211.32(a)). Congress clearly intended to empower bank-affiliated ETC's to export goods and services or facilitate the export of goods and services. Congress did not want bank-affiliated ETCs to engage in manufacturing or in agriculture, and said so clearly in the statute. But it had no intent to limit the services offered by bank-affiliated ETCs. Bank-affiliated ETCs possess distinct comparative advantages in dealing in services, and trade in services is as important to our future balance of trade position as trade in goods. Although you have called this matter to Chairman Volcker's attention, the FRB's response to your letters has not been adequate. In essence the FRB requires a bank-affiliated ETC to enter into a joint venture with an unaffiliated service company in order to export services. The joint venture often proves a very difficult and inefficient way to conduct international trade. The effect again is to reduce the effectiveness of ETCs, not encourage or promote them.

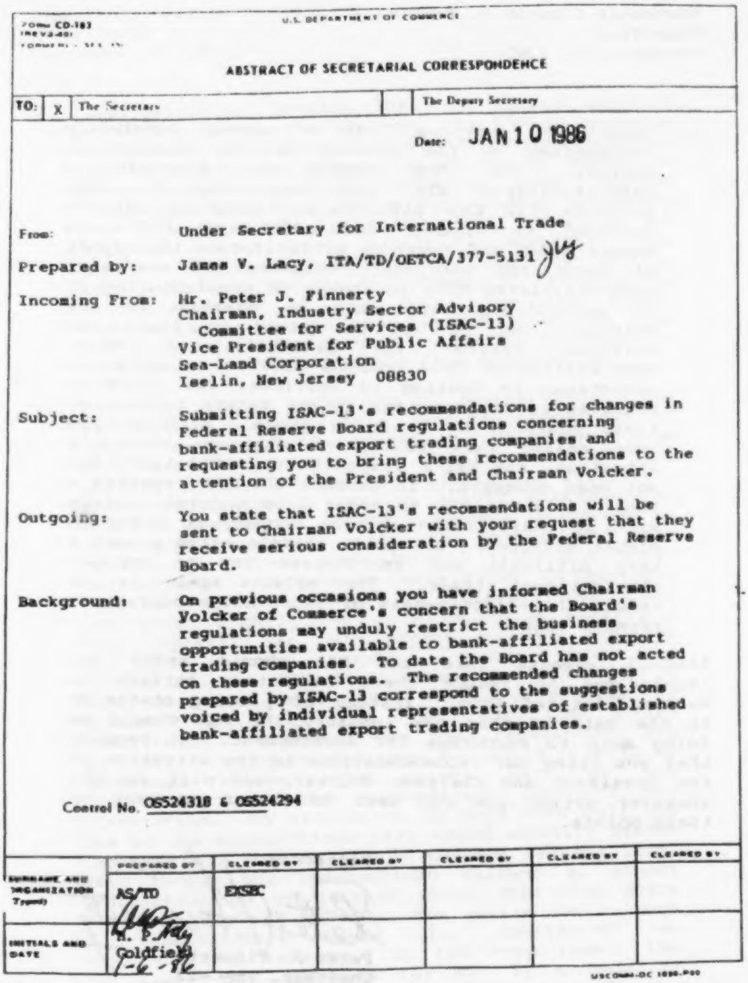
ISAC-13 submits that the FRB should amend its regulations to reduce these regulatory burdens on bank-affilitated ETCs. Instead of placing obstacles in the path of this new industry the FRB should be doing more to encourage ETC development. We request that you bring our recommendations to the attention of the President and Chairman Volcker, and will support whatever action you can take to foster progress on these points.

Sincerely,

Peter J. Finnerty

Peter J. Finnerty
Chairman, ISAC-13

cc: Secretary Malcolm Baldrige



FORM CD-183
(REV 3-80)

U.S. DEPARTMENT OF COMMERCE

ABSTRACT OF SECRETARIAL CORRESPONDENCE

TO: ☒ The Secretary ☐ The Deputy Secretary

Date: JAN 10 1986

From: Under Secretary for International Trade

Prepared by: James V. Lacy, ITA/TD/OETCA/377-5131 JVL

Incoming From: Mr. Peter J. Finnerty
Chairman, Industry Sector Advisory
Committee for Services (ISAC-13)
Vice President for Public Affairs
Sea-Land Corporation
Iselin, New Jersey 08830

Subject: Submitting ISAC-13's recommendations for changes in Federal Reserve Board regulations concerning bank-affiliated export trading companies and requesting you to bring these recommendations to the attention of the President and Chairman Volcker.

Outgoing: You state that ISAC-13's recommendations will be sent to Chairman Volcker with your request that they receive serious consideration by the Federal Reserve Board.

Background: On previous occasions you have informed Chairman Volcker of Commerce's concern that the Board's regulations may unduly restrict the business opportunities available to bank-affiliated export trading companies. To date the Board has not acted on these regulations. The recommended changes prepared by ISAC-13 correspond to the suggestions voiced by individual representatives of established bank-affiliated export trading companies.

Control No. 06524318 & 06524294

	PREPARED BY	CLEARED BY	CLEARED BY	CLEARED BY	CLEARED BY	CLEARED BY
SURNAME AND ORGANIZATION (Typed)	AS/TD	EXSEC				
INITIALS AND DATE	H. P. Goldfield 1-6-86					

USCOMM-DC 1890-P80

Export Promotion and Export Trading Companies

HYATT REGENCY CHICAGO
EAST TOWER GRAND BALLROOM

8:00 a.m.	**Continental Breakfast**
8:30 a.m.–8:40 a.m.	**Welcome** John J. Schornack, Managing Partner, Chicago Office, Arthur Young
8:40 a.m.–9:10 a.m.	**Introduction** H.P. Goldfield, Assistant Secretary for Trade Development, International Trade Administration, U.S. Department of Commerce
9:10 a.m.–10:30 a.m.	**Export Marketing Assistance—Government Programs and Commercial Services** Introduction: Joseph F. Christiano, Director, Chicago District Office, ITA, USDC Finding Export Markets: J.D. Honigberg, President, J.D. Honigberg International, and Director of Marshall International Trading Company Federal Programs for Agribusiness Exporters: Evans Browne, III, Chief, Program Operations Branch, USDA, Export Programs Division Exporter Services from the Private Sector: James Kalish, President and Managing Director of Panax Trading Company, Ltd. Questions and Answers
10:30 a.m.–10:45 a.m.	**Break**
10:45 a.m.–Noon	**Export Advantages & Obstacles: Trade Barriers Here and Abroad** **FSCs and Other Tax Issues: Matthew H. Paull, International Tax Specialist, Arthur Young** **Legal Issues in Agricultural Exporting:** Charles S. Levy, Mayer Brown & Platt, Washington, DC Anti-Trust Implications: Franklin P. Auwarter, Mayer Brown & Platt, Chicago Questions and Answers
Noon–2:00 p.m.	**Luncheon Speaker:** George D. Kennedy, President & Chief Executive Officer, International Minerals & Chemical Corporation, Northbrook, Illinois
2:00 p.m.–3:15 p.m.	**ETCs—Gaining a Competitive Edge: Transportation and Business Issues** Panel Discussion James V. Lacy, Director of the Office of Export Trading Company Affairs, USDC Martin F. (Buzz) Fitzpatrick, Director, Office of Transportation, USDA George Muller, Deputy Director of the Office of Export Trading Company Affairs, USDC Janice Payt, Attorney Advisor, Office of Asst. General Counsel for Trade Development, USDC Kay McLennan, Economist, Office of Transportation
3:15 p.m.–3:30 p.m.	**Break**
3:30 p.m.–5:00 p.m.	**Export Financing and Countertrade: Jets for Pigs and Other Deals** Introduction: David J. Paulus, Sr. Vice-President, The First National Bank of Chicago Panel Discussion Lynn K. Engstrand, Director, Agribusiness Countertrade, Northrup Corporation Leo G. Welt, President of Welt International Corporation Frank C. Schell III, Vice-President, The First National Bank of Chicago
5:00 p.m.–6:00 p.m.	**Cocktail Reception—Meet the Speakers**

Conference Highlights

The Conference agenda has been designed to allow for maximum interaction among attendees, the leaders of your industry, and the panel of expert speakers. Topics to be covered include the following:

INTERNATIONAL TRADE STRATEGIES

The ETC Act of 1982 will be re-examined following the recent publication of Final Regulations replacing Interim Rules in effect since April 1983. The greatly expanded guidelines explaining the implementation of regulations will be reviewed with emphasis on the interpretation of certification standards as set forth in the ETC Act. Questions relating to technology licensing involving export trade, "horizontal" and "vertical" conduct by exporters, and the protection provided by certificates for export as well as involvement in U.S. government financing are reviewed.

Provisions of Foreign Sales Corporations (FSC), the new trade support mechanism replacing the DISC, will be examined to determine their interaction with ETC Act provisions and foreign laws, and to insure their effective implementation into the structure of your export business as well as criteria for meeting the foreign presence test.

Lastly, Countertrade as a challenging trade mechanism with vastly increased importance to U.S.A. exporters will be examined by experienced practitioners. The role of Countertrade as a component of the global operations of major traders, their proven techniques, its impact on traditional overseas marketing, and aid in developing strategies for meeting Countertrade requirements, are among the objectives of this conference.

WHO SHOULD ATTEND

This conference will serve those businesses interested in the development of new strategies to handle the growing requirements of international trade. Large, as well as small- and medium-sized businesses, trade associations, primary service industries and individuals will be interested in the practical application of these new business opportunities. Corporate officials responsible for taxation, financial or international planning and development should attend this all-day conference. It is a one-stop opportunity to learn the up-to-date rules appropriate to the formation and use of ETCs, the advantages of establishing a FSC tax mechanism, as well as the development of expertise to meet the challenges of Countertrade prosper

PROGRAM

8:30 Registration/Coffee and Danish

9:15 Welcome
Al Nadler, Acting Director
N.Y. District Office, U.S. Dept. of Commerce
Morning Moderator
Steven E. Woolley, Executive Manager
U.S. Chamber of Commerce Northeast Region

9:25 "Export Trading Company Act Update"
James V. Lacy, Director
Office of Export Trading Company Affairs
U.S. Dept. of Commerce

9:45 "[illegible] Export Trade"
William B. Flynn, Partner
Ernst & Whinney

10:05 "Making [illegible] Together"
John C. Wagner, Attorney Advisor
Office of General Counsel
U.S. Dept. of Commerce

10:25 Questions and Answers

10:45 Coffee Break

11:00 "Your Bank's [illegible] Strategy"
Malcolm P. Davies, Vice President
Manufacturers Hanover Trust Company

11:20 "Countertrade: A U.S. View"
Frederic E. Howell, International Economist
U.S. Dept. of Commerce

11:40 "Organizing for Countertrade"
Frank A. Ocwieja, Vice President
M.G. Services, Inc.

12:00 Questions and Answers

12:30 Reception hosted by Ernst & Whinney

1:00 Luncheon
Keynote Address:
"U.S. Challenges of the 80's in International Trade"
Anna Chennault, President
TAC International, Inc.

2:30 "The Application of ETCs to Countertrade"
Mary Wadsworth Darby, Director — China
Sears World Trade, Inc.

2:50 Questions and Answers

3:15 Panel: "Utilizing Trade Mechanisms in Overseas Markets"
Moderator: James V. Lacy
Panelists: M.W. Darby, Sears World Trade
M.P. Davies, Manufacturers Hanover
W.B. Flynn, Ernst & Whinney
F.E. Howell, U.S. Dept. of Commerce
F.A. Ocwieja, M.G. Services
J.C. Wagner, U.S. Dept. of Commerce

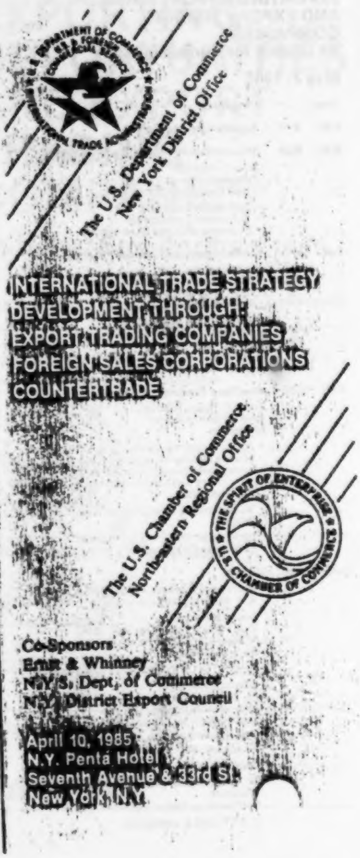
4:30 Adjourn

KEYNOTE ADDRESS BY ANNA CHENNAULT

At this conference on *International Trade Strategy Development Through the Application of Export Trading Companies, Foreign Sales Corporations and Countertrade*, Mrs. Anna Chennault will deliver the keynote address on "US Challenges of the 80's in International Trade."

As President of her own company, TAC International, Inc. and as Vice-Chairperson of President Reagan's Export Council, Mrs. Chennault has spoken to various organizations on international affairs and U.S. trade issues. She has been the President's envoy to many countries since 1981 and was recently a co-leader on a presidential trade mission for the aerospace industry to Japan, the People's Republic of China, Hong Kong and Taiwan. Last year she led a trade mission to Southeast Asia visiting Malaysia, the Philippines, Singapore, Thailand and Indonesia. She also travels extensively in the United States to promote U.S. export and international relations with our foreign trading partners.

An American citizen and resident of Washington, D.C., Mrs. Chennault has been a political leader for more than twenty years. She has been selected as "one of America's 75 most important women" by a national magazine and received honorary doctorate degrees from Chung-ang University, American University of the Caribbean and St. John's University. The President of St. John's University praised Anna Chennault as a "renaissance woman who has distinguished herself as a businesswoman, an aviation expert, writer, lecturer, statesperson, political force and patron [illegible] arts."



The U.S. Department of Commerce
New York District Office

INTERNATIONAL TRADE STRATEGY
DEVELOPMENT THROUGH:
EXPORT TRADING COMPANIES
FOREIGN SALES CORPORATIONS
COUNTERTRADE

The U.S. Chamber of Commerce
Northeastern Regional Office

Co-Sponsors
Ernst & Whinney
N.Y.S. Dept. of Commerce
N.Y. District Export Council

April 10, 1985
N.Y. Penta Hotel
Seventh Avenue & 33rd St.
New York, N.Y.

EXPORTING OPPORTUNITIES AND EXPORT TRADING COMPANIES:
An Update for Agribusiness

May 7, 1985

Time	Segment
8:00 - 8:45	**Registration and Coffee**
8:45 - 9:00	***Introduction to Program and Panelists*** John L. Hontalas Partner-in-Charge DH&S Monterey County • Benefits of Exporting • Purpose of Conference • Overview of Conference Agenda
9:00 - 9:45	***Market Leads and Market Potential*** Evans Browne Chief, Program Operations Branch Export Program Division, FAS U.S. Department of Agriculture • A View of the Marketplace • Where to Get Information and Help • AIMS • TELENET, AGRISTAR, AGNET • Other Sources of Market Information
9:45 - 12:00	***Business Planning and Financing*** Grant E. Rollin, Partner DH&S San Francisco Moderator • Planning techniques including consideration of alternative organizational structures, development of pro forma financial statements and capitalization requirements. • Understanding Foreign Sales Corporations (FSCs) Leonard W. Rothchild, Jr., Partner DH&S San Francisco
10:30 - 10:45	**BREAK** • Risk considerations, Private Financing and Use of the Letters of Credit Jack Hart Vice President and Manager of the Corporate Trade Finance Center Bank of America • Role of The Central Bank For Cooperatives Wayne Anderson Sr. Vice President International Banking Division Central Bank for Cooperatives • Government Financial Assistance Programs (Eximbank, AID, etc.) • Countertrade in Agriculture Dr. Suzanne Stafford, PhD President Countertrade Resources QUESTIONS & ANSWERS
12:30 - 2:00	**LUNCH** David P. Bernstein Vice President - Fresh Fruit Marketing Sunkist, Inc.
2:15 - 3:15	***Gaining a Competitive Edge*** James V. Lacy Director, Office of Export Trading Company Affairs U.S. Department of Commerce George Muller Deputy Director, Office of Export Trading Company Affairs U.S. Department of Commerce Janice A. Payt Attorney-Advisor Office of Assistant General Counsel for Trade Development U.S. Department of Commerce Export Trading Company Act • Statutory Framework • Role of ETCs • Advantages and Examples • Use of Coops/ETCs
3:15 - 3:30	**BREAK**
3:30 - 4:30	***Transportation to the Export Market*** • Government programs in support of improved agricultural export transportation Martin F. "Buzz" Fitzpatrick, Jr. Director, Office of Transportation U.S. Department of Agriculture • Use of transport-oriented export trading companies and the new Shipping Act of 1984 Kay L. McLennan Economist, Office of Transportation U.S. Department of Agriculture • "Straight talk" by a shipper and a representative of a group of shippers concerning shipping requirements and available export transportation John Moore President Moore Marketing International, Inc.
4:30 - 5:00	***Conclusion/Wrap-Up Session With Questions and Answers***
6:15 - 8:30	***Reception*** Host - Deloitte Haskins & Sells hn Hontalas, Partner-in-Charge nterey County Office

Location
The seminar will be held at the Quail Lodge, 8205 Valley Greens Drive, Carmel, CA 93923 (3.5 miles east of Hwy. 1). Registration will begin at 8:00 A.M., Tuesday morning. Room accommodations may be made by contacting the Lodge at (408) 624-1581.

Registration
The $125 registration fee includes all seminar materials, the FTC Guidebook, seminar luncheon, refreshments and cocktails. The enclosed registration form may be completed and returned with your check, made payable to Deloitte Haskins & Sells. You may also call the Deloitte Haskins & Sells office in Monterey County (408) 757-2901 to reserve a place at the conference.

EXPORTING OPPORTUNITIES AND EXPORT TRADING COMPANIES:

An Update for Agribusiness

May 7, 1985 **Carmel, California**

Sponsored by:

U.S. Department of Commerce

International Trade Administration

U.S. Department of Agriculture

USDA Office of Transportation

Deloitte Haskins & Sells

Deloitte
Haskins+Sells

A Conference for Banks and
Bank Holding Companies on

New Export Opportunities

**Available Under
The Export Trading Company Act
of 1982**

The Westin Plaza Hotel
New York City
October 3, 1985

Export
Trading
Companies

Sponsored by:

The U.S. Department of Commerce
The U.S. Department of the Treasury
in association with
The New York State Bankers Association

AGENDA

Registration: Baroque Suite 8:30 - 9:00

I Welcome Remarks: 9:00 - 9:15

James V. Lacy, Director
Office of Export Trading Company Affairs
U.S. Department of Commerce

Brent W. Free, Acting Deputy Assistant
Secretary for Services
U.S. Department of Commerce

II Keynote Speech: 9:15 - 9:45

H. P. Goldfield
Assistant Secretary for Trade Development
U.S. Department of Commerce

III Export-Import Bank: 9:45 - 10:15

Rita M. Rodriguez, Director
Export-Import Bank of the United States

Coffee Break 10:15 - 10:30

IV Federal Panel: 10:30 - 11:30

Margery Waxman (moderator)
Deputy General Counsel
Department of the Treasury

Eleanor Roberts Lewis, Assistant General
Counsel for Trade Development
U.S. Department of Commerce

Ricki Tigert, Assistant General Counsel
Board of Governors
Federal Reserve System

George Muller, Deputy Director
Office of Export Trading Company Affairs
U.S. Department of Commerce

V Private Business Panel: 11:30 - 12:00

Andre H. Friedman, Attorney
Goetz & Fitzpatrick

Ralph Chew, President
Chew International Group

Robert J. D'Emilio
International Sales
Manager, DEMACO

VI Luncheon: Crystal Room 12:15 - 1:45

Speaker to be announced

The afternoon panel of officials from the bank ETC industry will discuss operational experiences, export trends, and policy considerations.

VII Bank ETC Panel: Session I Baroque Suite 2:00 - 3:00

James V. Lacy, Director (moderator)
Office of Export Trading Company Affairs

Larry Meyers, Jr., Managing Director
State Street Trade Development Corp., Inc.

Malcolm P. Davies, President & CEO
Manufacturers Hanover World Trade Corp.

A. Philip Ferzan
Senior Vice President
and General Manager
Fidelity Tradexport Corporation

Alfred Kellogg, Vice President
Citicorp International Trading Company and
Counsel for Citicorp Global Trade Division

Break 3:00 - 3:15

VIII Bank ETC Panel: Session II 3:15 - 4:15

IX Reception: Crystal Room 4:45

Cosponsored by the New York State Bankers Association

PARTICIPANTS

RALPH H. CHEW is President of the Chew International Group, which includes export trading companies and export management companies and has specialized in exporting food products and manufactured goods for over fifty years. Mr. Chew is also President of the National Association of Export Companies, Inc. and is Chairman of the National Federation of Export Associations.

MALCOLM P. DAVIES is President and CEO of the Manufacturers Hanover World Trade Corporation. Previously, he was Export Finance Manager for the Merchant Bank Hill Samuel and Company. Prior to that time, Mr. Davies held positions with the General Electric Company and the British Aircraft Corporation.

ROBERT J. D'EMILIO is International Sales Manager of DEMACO, manufacturer of a complete line of pasta products. He has traveled extensively on behalf of DEMACO, including visits to the Soviet Union, the People's Republic of China, Eastern Europe, Japan and Latin America.

A. PHILIP FERZAN is Senior Vice President and General Manager of Fidelity Tradexport Corporation, the export trading company that he organized for First Fidelity Bank under the 1982 ETC Act. Prior to joining First Fidelity in 1973, Mr. Ferzan held international banking positions with Citibank and the Marine Midland Bank.

BRANT W. FREE is Acting Deputy Assistant Secretary for Services in the Department of Commerce. Previously, Mr. Free worked in a number of program areas at the Department, including trade promotion, international regional economics, export finance, and international taxation. He was also Acting Deputy Assistant Secretary for Finance, Investment and Services.

ANDRE H. FRIEDMAN is a practicing attorney in New York City concentrating on international trade and business law with the firm of Goetz & Fitzpatrick. Previously he served as President of the Bard Group, an international trading organization which he founded in 1965. The firm specialized in supplying materials for major construction projects worldwide and served as the overseas export representative for American manufacturers.

H. P. GOLDFIELD is the Assistant Secretary of Commerce for Trade Development. In addition, Mr. Goldfield also serves on the Boards of Directors for the U. S. Export-Import Bank and the Overseas Private Investment Corporation. Prior to his appointment at the Commerce Department, Mr. Goldfield was a member of The White House staff serving as Assistant Counsel to the President (1981-83). Mr. Goldfield was formerly associated with the New York City law firms of Cadwalader, Wickersham & Taft and Schulte, Roth & Zabel. From 1975 to 1977, he served as Assistant and Law Clerk to Philip W. Buchen, Counsel to President Ford.

ALFRED KELLOGG is Vice President of Citicorp International Trading Company, Inc., and Division Counsel for the bank's Global Trade Division. Mr. Kellogg was previously a senior attorney with Pan American World Airways and an Associate with Hughes, Hubbard & Reed.

JAMES V. LACY is Director of the Office of Export Trading Company Affairs in the Department of Commerce. Prior to this appointment, Mr. Lacy served on Secretary Baldrige's staff as Deputy Director for Business Issues in the Department's Office of Business Liaison. Before joining Commerce, Mr. Lacy was a partner in a Los Angeles-based public affairs consulting firm. An attorney, Mr. Lacy is admitted to practice law in California and the District of Columbia.

ELEANOR ROBERTS LEWIS is Assistant General Counsel for Trade Development in the U.S. Department of Commerce. Ms. Lewis came into the job after three years as Assistant General Counsel for Finance at the U.S. Department of Housing and Urban Development. Before that she was associated with the Washington, D.C. law firm of Brownstein, Zeidman and Schomer.

LAWRENCE MEYERS, Jr. is a Managing Director of the State Street Trade Development Company, Inc., part of the State Street Boston Corporation. He is jointly responsible for the overall executive and financial management of the firm and is in charge of all corporate marketing activities. Before joining State Street Trade Development Company, Mr. Meyers was Director of Marketing for the computer products division of the Nashua Corporation. Earlier he was Vice President of Marketing for Systems Research Corporation.

GEORGE MULLER is Deputy Director of the Office of Export Trading Company Affairs in the Department of Commerce. Mr. Muller previously served as Deputy Assistant Secretary for Finance for the Commerce Department's Economic Development Administration, and as that agency's legal counsel in Austin, Texas.

RITA M. RODRIGUEZ is a Director of the Export-Import Bank of the United States. She taught at the University of Illinois from 1978 to 1982 and was Associate Professor of Business Administration at the Harvard Business School from 1969 to 1978. Dr. Rodriguez also lectured at New York University and was a research assistant with the National Bureau of Economic Research. She has served as a consultant in international finance to U.S. corporations and to U.S. and foreign government agencies.

RICKI TIGERT is Assistant General Counsel for International Banking at the Federal Reserve Board. Prior to assuming that position in May of this year, she was Senior Counsel for International Finance at the Department of the Treasury. Ms. Tigert has practiced law in Washington, worked as counsel to a Congressional committee, and clerked for Judge John Minor Wisdom of the U.S. Court of Appeals for the Fifth Circuit.

MARGERY WAXMAN is Deputy General Counsel of the Department of the Treasury where she had the lead responsibility for the Department in drafting and implementing the Export Trading Company Act. Previously, Ms. Waxman served as General Counsel in the Office of Personnel Management, Executive Director of the Federal Trade Commission, Deputy General Counsel for the Cost of Living Council and Assistant General Counsel for The White House's Office of Consumer Affairs, and as an Associate with Covington and Burling.

Mr. Barnard. Mr. Dahl, has the Fed reached a decision on the bill that was introduced by Senator Heinz?

Mr. Dahl. No; it hasn't, Mr. Chairman.

Mr. Barnard. Has it considered it at all?

Mr. Dahl. No; it hasn't. It is generally aware of what the provisions are.

Mr. Barnard. I understand also that you have not made a response to the GAO study?

Mr. Dahl. We made a response on the initial draft report of the GAO study, which is the normal procedure. That draft report did not contain any recommendations, and we have not seen the final report.

[Subcommittee note.—Relevant portions of the final GAO report were provided to the Federal Reserve 1½ weeks prior to the hearing.]

Mr. Barnard. Would you please furnish a copy of your response to the GAO on the final report?

Mr. Dahl. When it is done, we certainly will, Mr. Chairman.

[The information referred to follows:]

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

April 21, 1986

The Honorable Doug Barnard, Jr.
Chairman
Subcommittee on Commerce, Consumer
and Monetary Affairs
Committee on Government Operations
House of Representatives
Washington, D.C. 20515

Dear Chairman Barnard:

During Mr. Frederick R. Dahl's testimony on March 4, 1986, before your Subcommittee regarding the Board's implementation of the Bank Export Services Act, you requested a copy of the Board's response to the final version of the GAO report on this subject. You may recall that during the hearing attention was called to the fact that material changes had been made to the report on which the Board had not been given an opportunity to comment.

The Board has now reviewed the final version of the GAO report, and I am pleased to enclose a copy of the Board's response.

Please let me know if I can be of further assistance.

Sincerely

Don Winn

Donald J. Winn
Assistant to the Board

Enclosure

RECEIVED
APR 22 1986
COMMERCE, CONSUMER AND
MONETARY AFFAIRS SUBCOMMITTEE

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

APR 21 1986

Mr. William J. Anderson
Director, General Government Division
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Anderson,

The Board of Governors has now received the final version of the General Accounting Office ("GAO") report on "Implementation of the Export Trading Company Act of 1982." The final version differs in two material respects from the draft report on which the Board offered comments last December.

The first difference is inclusion of the suggestion that the Board could, consistent with the statute, amend the test established to determine whether an Export Trading Company ("ETC") is organized and operated "principally" for exporting and facilitating exports. A second difference in the report is the insertion of the conclusion that the Board's rule limiting the export of services by ETCs is not a proper interpretation of the statute and its legislative history.

Criticisms of the Board's rules along these lines are not new, having been offered a number of times from within the industry. The Board's views on these criticisms have been presented in testimony before a subcommittee of the House Foreign Affairs Committee in June 1984, in a report to the Congress on implementation of the Bank Export Services Act in October 1984, and again in testimony before a subcommittee of the House Committee on Government Operations in March 1986.

With respect to the first suggestion, the final report states that the Board could (1) include only proceeds from U.S. exports and imports for purposes of the test, thus excluding proceeds from third country trade; (2) devise indices in addition to revenue to determine whether the statutory test is met; and (3) extend the period for meeting the test beyond two years. The Board continues to believe that to exclude revenues derived from third country trade would allow, and would likely result in, ETC's owned by banking organizations being primarily or predominately engaged in trading activities unrelated to exports from the United States. The Board submits that this result would be a clear contravention of Congressional intent that bank affiliated ETC's should promote or facilitate the export of goods and services from the United States. A reflection of this intent may be found in 128 Cong. Rec. H8464 (daily ed. Oct. 1, 1982).

William Anderson

On devising indices other than revenues for the purpose of measuring the export activity of ETCs, it may be noted that this provision was published for comment before the Board's ETC rules were adopted. Among the comments received, there were differences on the way a revenues test should be applied, but there was general concurrence that revenues offered an appropriate measure of trade activity. The GAO report does not recommend or suggest any index of activity to be used in place of or in addition to revenues.

With respect to the period for meeting the revenues test, the Board had originally suggested a one year period. This was extended to two years in the final regulation, which further stated that when the revenues test was not met, an ETC should notify the Board of the reasons for noncompliance and develop an adequate plan for meeting the requirement. So far, no ETC has notified the Board that it has not met the test. Thus the Board has yet to consider a practical case involving this rule.

As for allowing bank-affiliated ETC's to provide foreign residents with any and all kinds of services, the result might be that these ETCs would obtain earnings from foreigners. However, the consequence would not necessarily be an export of services from the United States, nor an increase in U.S. jobs related to the provision of services. The intention of Congress is quite clear that bank-affiliated ETCs, with their established networks of foreign offices, should be intermediaries in the export of U.S. goods and services, rather than primary providers of services to foreigners. For example, in commenting on the legislation, Representative Barnard stated:

> "Export trading companies . . . will be able to provide services to the smaller and medium-sized exporter that are currently available only to huge corporations. Utilizing the expertise and foreign presence of banks, they will be able to package export services ranging from marketing surveys to finding buyers, from arranging shipping to product modification, and from financing payment to arranging barter transactions. In all cases, these are services that presently are available only to those exporters who are able to devote the time and money to search them out." 128 Cong. Rec. H8462 (daily ed. Oct. 1, 1982)

Indeed, the statute itself, in Title I, recognizes that ETCs are intended to function as intermediaries:

> "The Congress finds that . . . the United States needs well-developed export trade intermediaries which can achieve economies of scale and acquire expertise enabling them to export goods and services profitably, at low per unit cost to producers." (Emphasis added)
> 15 U.S.C. 4001 (a) (7)

The Board believes that the rules discussed in this letter represent the proper interpretation of Congressional intent in enacting legislation allowing bank holding companies to own or invest in ETCs as a means of promoting U.S. exports.

Very truly yours,

(signed) William W. Wiles

William W. Wiles
Secretary of the Board

Mr. **Barnard**. Mr. Dahl, how often do the Federal Reserve examiners inspect bank ETC's?

Mr. **Dahl**. Inspections of bank ETC's are generally conducted in connection with the examination of the bank holding company itself, and in the past we have sought to examine these on an annual basis. Our whole examination procedure for bank holding companies and banks is under review at the present time, but that is roughly the time interval that has occurred in these examinations. To date, 24 ETC's owned by bank holding companies have been inspected.

Mr. **Barnard**. Without being specific as to any bank, of course, because that's confidential, what general problems have you uncovered in the examination of ETC's—bank ETC's?

Mr. **Dahl**. I think there's a reference here in my statement, Mr. Chairman, about several cases where we have noted problems in them or they have really lost a great deal of money. I think there were four instances where they lost a great deal of money. For example, a major customer broke the terms of its trade agreement, and another one lost all of its capital because of its inability to deliver, and others have encountered losses, and some of these losses have wiped out the capital of some of these ETC's.

Most of them, as I've indicated, have been only semiactive, if not dormant, and consequently there has not been much to find to criticize in their performance or major problems, but there have been these problems with startup costs and an unfavorable environment which have maintained their expenses but not brought in any revenues.

Mr. **Barnard**. Mr. Dahl, Mr. Rice of Chase Trade, Inc., suggested earlier today in his testimony that the Federal Reserve Board establish an Office of Export Trading Companies, primarily a task force of existing staff, to conduct seminars, do staff studies on export trading companies, and educate Federal Reserve staff. What is your response to this suggestion?

Mr. **Dahl**. Well, I haven't had time to consider that thoroughly, but it would certainly mark a considerable change from the role the Board has envisaged for itself in the supervision of bank-owned export trading companies, and certainly, we think, from that which was envisioned by the Congress in the original legislation. It was rather clear to us that the Congress envisioned us to be a rather passive participant in this process, largely concerned with any implications that the export trading company might have for the health and soundness of the associated bank. I'm having great difficulties, mentally, Mr. Chairman, in envisioning how we would operate in that fashion.

Mr. **Barnard**. I think that his purpose was more to acquaint the Federal Reserve staff on the operation of ETC's, in order that your policies and regulations as well as the day to day operations of ETC's would be better understood.

I can understand that this is a new act, this is a new endeavor for banks and bank holding companies, and even the regulators sometimes have some difficulty in coping with this so-called new change. I know today we have repeatedly heard references to the Glass-Steagall Act as far as the ETC's are concerned. So we know that there is still hovering over this whole climate some great fears that we had in the 1930's—you know, a complete undeniable separation of banking and commerce is the salvation of this country—and yet we find today that it is being violated often.

I can see where the Fed staff could very well understand the relationship of banks and their role in this trading business, and at the same time don't quite understand that banks are not really in commerce but that they are financing commerce; that they have a very, very small risk, if any at all, in assets and capital in the ETC's operation. But it's a marriage of traders and finance which we sorely need today if we are going to correct this export market.

Mr. **Dahl**. Let me respond to that, Mr. Chairman, by saying, first of all, that there is doubtless more that we can do to learn about the operations and the particular difficulties of export trading companies that are owned by banks. But we have, as Mr. Lacy said, participated in a number of conferences that the Commerce Department has sponsored and others have sponsored to mingle with industry, so to speak, and get reactions, and we have sought to maintain contacts with the banks themselves and their export trading companies. I have in the past, myself, talked to Mr. Rice and others about this.

On the other question you are raising, which is a much broader question that has to do with the boundaries of the permissible activities of banks in relation to commercial enterprises, it is on those boundary questions where I think that the Board has understandably been a little more cautious. We have been much more relaxed about export trading companies in the financing business since that's something that banks know something about or are supposed to know something about and are familiar with. As I said, as you get into these boundaries where we have been more cautious and have wanted to review and see what is happening——

Mr. **Barnard**. Your Chairman came before our Banking Committee last week, and he challenged us to do something about the financial structure of the country. I don't back off from that. I think Congress ought to address it after some 4 or 5 years of doing nothing and watching the courts, and the State governments, and even the regulators, who can't get together on anything, attempt to do something—all of those involved in the financial structure. So I'm very interested in how we are going. But that's another subject.

Mr. **Dahl**. Yes.

Mr. **Barnard**. What are the Federal Reserve Board's manpower resources allocated to bank ETC's?

Mr. **Dahl**. Well, they are not very large, Mr. Chairman. As I've said, we've had 40 notifications to establish ETC's, and we've had 8 other applications amending their original proposals. These have been processed in the context of the usual applications, procedures at the Board, so that what occurs actually is that this amounts to a very small fraction of the time of our analysts.

Mr. **Barnard**. You're just waiting for the activity to increase the staff then?

Mr. **Dahl**. Pardon?

Mr. **Barnard**. You're just waiting for the activity to increase the staff.

Mr. **Dahl**. Well, it's clearly a collateral duty for the analysts on the staffs of the Reserve banks and the Board. There are usually at the Reserve banks a couple of analysts and a couple of lawyers who look at the applications as they come in, and it's about the same number that look at them when they reach the Board, at least those that do reach the Board.

As I said, at the inspection level, this is done in conjunction with the inspection of the bank holding company inspections. So this is only a small portion of the manpower devoted to them, and I can't give you a better estimate of what that would be at the present time.

Mr. **Barnard**. This limited staff of course—is that the reason it took 11 months to have Chase's application to get a waiver?

Mr. **Dahl**. I'm unfamiliar that it took 11 months. By the time they put in an application, we have a rule that everything is acted on within 60 days, and that one was acted on in approximately that length of time. Whether they started talking to the Reserve bank when this was first a gleam in their eye or an actual proposition I cannot say.

Mr. **Barnard**. I have to say, our staff may have made an error. You know, the staffs don't normally make errors, but they sometimes have. It was 4 months. In fact, your statement's appendix states it was 4 months, Chase Trade said it was 11 months, but we won't quibble over 7 months.

[SUBCOMMITTEE NOTE.—Mr. Rice sent the following letter to clear up the discrepancy:]

Chase Trade, Inc.
One World Trade Center-78th Floor
New York, New York 10048

R. Michael Rice
President

CHASE

RECEIVED
MAR 17 1986
COMMERCE, CONSUMER AND
MONETARY AFFAIRS SUBCOMMITTEE

March 12, 1986

Mr. Stephen R. McSpadden
Counsel
Committee on Government Operations
Rayburn House Office Building, Room B-377
Washington, DC 20515

Dear Steve:

It was indeed a pleasure to appear before the Subcommittee on Government Operations on March 4 to testify on the Export Trading Company Act and the Federal Reserve Board's regulations. In that regard you asked me to clarify some points I made regarding the experience we had in requesting approval to increase our leverage from no greater than 10:1 to an amount no greater than 17:1.

In my testimony I indicated that the process was time consuming, frought with uncertainty and that the approval was conditional. Let me emphasize that I do not want to appear critical of the Federal Reserve. Our experience is that it is an institution distinguished by its professionalism and a very fine staff. However, given the nature of the regulatory process, ETCs would be better off and more competitive if they did not need to go through the steps needed to get waivers to regulations for so many of the day-to-day powers that our competitors enjoy without regulatory hurdles.

Our counsel contacted the Federal Reserve Bank in early April 1985 to inform them of our intent to increase leverage from 10:1 to 17:1. Counsel's memo of April 11, 1985 summarizing the FRB meeting indicates that we were advised that an application to the Board of Governors in Washington would be necessary before we could increase our leverage. The New York Reserve Bank further indicated "severe reservation about the success of Chase Trade's application," adding that those applicants who had requested in excess of 10:1 in their de novo applications had all been limited to 10:1. In an effort to prepare an informationally adequate application several drafts were circulated internally and additional phone conversations held with FRB staff. On June 24, 1985, the Federal Reserve Bank of New York acknowledged receipt of our draft application and posed additional questions. On September 26, 1985 a final application was filed; this was acknowledged by the Reserve Bank on October 16 and additional questions were asked. We answered those questions on October 28. Our application was forwarded to the Board in Washington and during the next months several phone conversations were held with both the Reserve Bank and Board staff in Washington. We received final approval of our leverage request on March 6 by letter dated February 26. I should point out that the approval is conditioned on our following certain financial and commercial procedures.

I appreciate the opportunity to make our views known. Please call if I can answer any further questions.

Sincerely,

cc: John Doherty

Mr. **Barnard**. Thank you very much for being here this morning, gentlemen. We appreciate your testimony and the participation.

Mr. Dahl, if you would, if you could furnish a copy of your response; and, Mr. Lacy, if you have any further information with reference to this bill, we would appreciate it very much.

With that, the committee is adjourned.

[Whereupon, at 1:40 p.m., the subcommittee adjourned, to reconvene subject to the call of the Chair.]

APPENDIXES

Appendix 1.—Statutory Provisions of the Export Trading Company Act of 1982

Public Law 97-290
97th Congress

An Act

To encourage exports by facilitating the formation and operation of export trading companies, export trade associations, and the expansion of export trade services generally.

Oct. 8, 1982
[S. 734]

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

Export trade services, expansion.
Export Trading Company Act of 1982.

TITLE I—GENERAL PROVISIONS

SHORT TITLE

SEC. 101. This title may be cited as the "Export Trading Company Act of 1982".

15 USC 4001 note.

FINDINGS; DECLARATION OF PURPOSE

SEC. 102. (a) The Congress finds that—

15 USC 4001.

(1) United States exports are responsible for creating and maintaining one out of every nine manufacturing jobs in the United States and for generating one out of every seven dollars of total United States goods produced;

(2) the rapidly growing service-related industries are vital to the well-being of the United States economy inasmuch as they create jobs for seven out of every ten Americans, provide 65 per centum of the Nation's gross national product, and offer the greatest potential for significantly increased industrial trade involving finished products;

(3) trade deficits contribute to the decline of the dollar on international currency markets and have an inflationary impact on the United States economy;

(4) tens of thousands of small- and medium-sized United States businesses produce exportable goods or services but do not engage in exporting;

(5) although the United States is the world's leading agricultural exporting nation, many farm products are not marketed as widely and effectively abroad as they could be through export trading companies;

(6) export trade services in the United States are fragmented into a multitude of separate functions, and companies attempting to offer export trade services lack financial leverage to reach a significant number of potential United States exporters;

(7) the United States needs well-developed export trade intermediaries which can achieve economies of scale and acquire expertise enabling them to export goods and services profitably, at low per unit cost to producers;

(8) the development of export trading companies in the United States has been hampered by business attitudes and by Government regulations;

(9) those activities of State and local governmental authorities which initiate, facilitate, or expand exports of goods and serv-

ices can be an important source for expansion of total United States exports, as well as for experimentation in the development of innovative export programs keyed to local, State, and regional economic needs;

(10) if United States trading companies are to be successful in promoting United States exports and in competing with foreign trading companies, they should be able to draw on the resources, expertise, and knowledge of the United States banking system, both in the United States and abroad; and

(11) the Department of Commerce is responsible for the development and promotion of United States exports, and especially for facilitating the export of finished products by United States manufacturers.

(b) It is the purpose of this Act to increase United States exports of products and services by encouraging more efficient provision of export trade services to United States producers and suppliers, in particular by establishing an office within the Department of Commerce to promote the formation of export trade associations and export trading companies, by permitting bank holding companies, bankers' banks, and Edge Act corporations and agreement corporations that are subsidiaries of bank holding companies to invest in export trading companies, by reducing restrictions on trade financing provided by financial institutions, and by modifying the application of the antitrust laws to certain export trade.

USC 181 note.

DEFINITIONS

JSC 4002. SEC. 103. (a) For purposes of this title—

(1) the term "export trade" means trade or commerce in goods or services produced in the United States which are exported, or in the course of being exported, from the United States to any other country;

(2) the term "services" includes, but is not limited to, accounting, amusement, architectural, automatic data processing, business, communications, construction franchising and licensing, consulting, engineering, financial, insurance, legal, management, repair, tourism, training, and transportation services;

(3) the term "export trade services" includes, but is not limited to, consulting, international market research, advertising, marketing, insurance, product research and design, legal assistance, transportation, including trade documentation and freight forwarding, communication and processing of foreign orders to and for exporters and foreign purchasers, warehousing, foreign exchange, financing, and taking title to goods, when provided in order to facilitate the export of goods or services produced in the United States;

(4) the term "export trading company" means a person, partnership, association, or similar organization, whether operated for profit or as a nonprofit organization, which does business under the laws of the United States or any State and which is organized and operated principally for purposes of—

(A) exporting goods or services produced in the United States; or

(B) facilitating the exportation of goods or services produced in the United States by unaffiliated persons by providing one or more export trade services;

(5) the term "State" means any of the several States of the United States, the District of Columbia, the Commonwealth of Puerto Rico, the Virgin Islands, American Samoa, Guam, the Commonwealth of the Northern Mariana Islands, and the Trust Territory of the Pacific Islands;

(6) the term "United States" means the several States of the United States, the District of Columbia, the Commonwealth of Puerto Rico, the Virgin Islands, American Samoa, Guam, the Commonwealth of the Northern Mariana Islands, and the Trust Territory of the Pacific Islands; and

(7) the term "antitrust laws" means the antitrust laws as defined in subsection (a) of the first section of the Clayton Act (15 U.S.C. 12(a)), section 5 of the Federal Trade Commission Act (15 U.S.C. 45) to the extent that section 5 applies to unfair methods of competition, and any State antitrust or unfair competition law.

(b) The Secretary of Commerce may by regulation further define any term defined in subsection (a), in order to carry out this title.

OFFICE OF EXPORT TRADE IN DEPARTMENT OF COMMERCE

15 US

SEC. 104. The Secretary of Commerce shall establish within the Department of Commerce an office to promote and encourage to the greatest extent feasible the formation of export trade associations and export trading companies. Such office shall provide information and advice to interested persons and shall provide a referral service to facilitate contact between producers of exportable goods and services and firms offering export trade services.

TITLE II—BANK EXPORT SERVICES

Bank
Servic

SHORT TITLE

12 US
note.

SEC. 201. This title may be cited as the "Bank Export Services Act".

12 US
note.
30 US

Post, p.
12 USC

SEC. 202. The Congress hereby declares that it is the purpose of this title to provide for meaningful and effective participation by bank holding companies, bankers' banks, and Edge Act corporations, in the financing and development of export trading companies in the United States. In furtherance of such purpose, the Congress intends that, in implementing its authority under section 4(c)(14) of the Bank Holding Company Act of 1956, the Board of Governors of the Federal Reserve System should pursue regulatory policies that—

(1) provide for the establishment of export trading companies with powers sufficiently broad to enable them to compete with similar foreign-owned institutions in the United States and abroad;

(2) afford to United States commerce, industry, and agriculture, especially small- and medium-size firms, a means of exporting at all times;

(3) foster the participation by regional and smaller banks in the development of export trading companies; and

(4) facilitate the formation of joint venture export trading companies between bank holding companies and nonbank firms that provide for the efficient combination of complementary

trade and financing services designed to create export trading companies that can handle all of an exporting company's needs.

INVESTMENTS IN EXPORT TRADING COMPANIES

SEC. 203. Section 4(c) of the Bank Holding Company Act of 1956 (12 U.S.C. 1843(c)) is amended—

(1) in paragraph (12)(B), by striking out "or" at the end thereof;

(2) in paragraph (13), by striking out the period at the end thereof and inserting in lieu thereof "; or"; and

(3) by inserting after paragraph (13) the following:

"(14) shares of any company which is an export trading company whose acquisition (including each acquisition of shares) or formation by a bank holding company has not been disapproved by the Board pursuant to this paragraph, except that such investments, whether direct or indirect, in such shares shall not exceed 5 per centum of the bank holding company's consolidated capital and surplus.

"(A)(i) No bank holding company shall invest in an export trading company under this paragraph unless the Board has been given sixty days' prior written notice of such proposed investment and within such period has not issued a notice disapproving the proposed investment or extending for up to another thirty days the period during which such disapproval may be issued.

"(ii) The period for disapproval may be extended for such additional thirty-day period only if the Board determines that a bank holding company proposing to invest in an export trading company has not furnished all the information required to be submitted or that in the Board's judgment any material information submitted is substantially inaccurate.

"(iii) The notice required to be filed by a bank holding company shall contain such relevant information as the Board shall require by regulation or by specific request in connection with any particular notice.

"(iv) The Board may disapprove any proposed investment only if—

"(I) such disapproval is necessary to prevent unsafe or unsound banking practices, undue concentration of resources, decreased or unfair competition, or conflicts of interest;

"(II) the Board finds that such investment would affect the financial or managerial resources of a bank holding company to an extent which is likely to have a materially adverse effect on the safety and soundness of any subsidiary bank of such bank holding company, or

"(III) the bank holding company fails to furnish the information required under clause (iii).

"(v) Within three days after a decision to disapprove an investment, the Board shall notify the bank holding company in writing of the disapproval and shall provide a written statement of the basis for the disapproval.

"(vi) A proposed investment may be made prior to the expiration of the disapproval period if the Board issues

written notice of its intent not to disapprove the investment.

"(B)(i) The total amount of extensions of credit by a bank holding company which invests in an export trading company, when combined with all such extensions of credit by all the subsidiaries of such bank holding company, to an export trading company shall not exceed at any one time 10 per centum of the bank holding company's consolidated capital and surplus. For purposes of the preceding sentence, an extension of credit shall not be deemed to include any amount invested by a bank holding company in the shares of an export trading company.

"(ii) No provision of any other Federal law in effect on October 1, 1982, relating specifically to collateral requirements shall apply with respect to any such extension of credit.

"(iii) No bank holding company or subsidiary of such company which invests in an export trading company may extend credit to such export trading company or to customers of such export trading company on terms more favorable than those afforded similar borrowers in similar circumstances, and such extension of credit shall not involve more than the normal risk of repayment or present other unfavorable features.

"(C) For purposes of this paragraph, an export trading company—

"(i) may engage in or hold shares of a company engaged in the business of underwriting, selling, or distributing securities in the United States only to the extent that any bank holding company which invests in such export trading company may do so under applicable Federal and State banking laws and regulations; and

"(ii) may not engage in agricultural production activities or in manufacturing, except for such incidental product modification including repackaging, reassembling or extracting byproducts, as is necessary to enable United States goods or services to conform with requirements of a foreign country and to facilitate their sale in foreign countries.

"(D) A bank holding company which invests in an export trading company may be required, by the Board, to terminate its investment or may be made subject to such limitations or conditions as may be imposed by the Board, if the Board determines that the export trading company has taken positions in commodities or commodity contracts, in securities, or in foreign exchange, other than as may be necessary in the course of the export trading company's business operations.

"(E) Notwithstanding any other provision of law, an Edge Act corporation, organized under section 25(a) of the Federal Reserve Act (12 U.S.C. 611-631), which is a subsidiary of a bank holding company, or an agreement corporation, operating subject to section 25 of the Federal Reserve Act (12 U.S.C. 601-604(a)), which is a subsidiary of a bank holding company, may invest directly and indirectly in the aggregate up to 5 per centum of its consolidated capital and

surplus (25 per centum in the case of a corporation not engaged in banking) in the voting stock of other evidences of ownership in one or more export trading companies.

ions.

"(F) For purposes of this paragraph—

"(i) the term 'export trading company' means a company which does business under the laws of the United States or any State, which is exclusively engaged in activities related to international trade, and which is organized and operated principally for purposes of exporting goods or services produced in the United States or for purposes of facilitating the exportation of goods or services produced in the United States by unaffiliated persons by providing one or more export trade services.

"(ii) the term 'export trade services' includes, but is not limited to, consulting, international market research, advertising, marketing, insurance (other than acting as principal, agent or broker in the sale of insurance on risks resident or located, or activities performed, in the United States, except for insurance covering the transportation of cargo from any point of origin in the United States to a point of final destination outside the United States), product research and design, legal assistance, transportation, including trade documentation and freight forwarding, communication and processing of foreign orders to and for exporters and foreign purchasers, warehousing, foreign exchange, financing, and taking title to goods, when provided in order to facilitate the export of goods or services produced in the United States;

"(iii) the term 'bank holding company' shall include a bank which (I) is organized solely to do business with other banks and their officers, directors, or employees; (II) is owned primarily by the banks with which it does business; and (III) does not do business with the general public. No such other bank, owning stock in a bank described in this clause that invests in an export trading company, shall extend credit to an export trading company in an amount exceeding at any one time 10 per centum of such other bank's capital and surplus; and

"(iv) the term 'extension of credit' shall have the same meaning given such term in the fourth paragraph of section 23A of the Federal Reserve Act.".

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SC 1843

SEC. 205. On or before two years after the date of the enactment of this Act, the Federal Reserve Board shall report to the Committee on Banking, Housing, an Urban Affairs of the Senate and the Committee on Banking, Finance and Urban Affairs of the House of Representatives the Board's recommendations with respect to the implementation of this section, the Board's recommendations on any changes in United States law to facilitate the financing of United States exports, especially by small, medium-size, and minority business concerns, and the Board's recommendations on the effects of ownership of United States banks by foreign banking organizations affiliated with trading companies doing business in the United States.

GUARANTEES FOR EXPORT ACCOUNTS RECEIVABLE AND INVENTORY

SEC. 206. The Export-Import Bank of the United States is authorized and directed to establish a program to provide guarantees for loans extended by financial institutions or other public or private creditors to export trading companies as defined in section 4(c)(14)(F)(i) of the Bank Holding Company Act of 1956, or to other exporters, when such loans are secured by export accounts receivable or inventories of exportable goods, and when in the judgment of the Board of Directors— *Ante*, p. 1

(1) the private credit market is not providing adequate financing to enable otherwise creditworthy export trading companies or exporters to consummate export transactions; and

(2) such guarantees would facilitate expansion of exports which would not otherwise occur.

The Board of Directors shall attempt to insure that a major share of any loan guarantees ultimately serves to promote exports from small, medium-size, and minority businesses or agricultural concerns. Guarantees provided under the authority of this section shall be subject to limitations contained in annual appropriations Acts.

BANKERS' ACCEPTANCES

SEC. 207. The seventh paragraph of section 13 of the Federal Reserve Act (12 U.S.C. 372) is amended to read as follows: 12 USC 372

"(7)(A) Any member bank and any Federal or State branch or agency of a foreign bank subject to reserve requirements under section 7 of the International Banking Act of 1978 (hereinafter in this paragraph referred to as 'institutions'), may accept drafts or bills of exchange drawn upon it having not more than six months' sight to run, exclusive of days of grace—

"(i) which grow out of transactions involving the importation or exportation of goods;

"(ii) which grow out of transactions involving the domestic shipment of goods; or

"(iii) which are secured at the time of acceptance by a warehouse receipt or other such document conveying or securing title covering readily marketable staples.

"(B) Except as provided in subparagraph (C), no institution shall accept such bills, or be obligated for a participation share in such bills, in an amount equal at any time in the aggregate to more than 150 per centum of its paid up and unimpaired capital stock and surplus or, in the case of a United States branch or agency of a foreign bank, its dollar equivalent as determined by the Board under subparagraph (H).

"(C) The Board, under such conditions as it may prescribe, may authorize, by regulation or order, any institution to accept such bills, or be obligated for a participation share in such bills, in an amount not exceeding at any time in the aggregate 200 per centum of its paid up and unimpaired capital stock and surplus or, in the case of a United States branch or agency of a foreign bank, its dollar equivalent as determined by the Board under subparagraph (H).

"(D) Notwithstanding subparagraphs (B) and (C), with respect to any institution, the aggregate acceptances, including obligations for a participation share in such acceptances, growing out of domestic transactions shall not exceed 50 per centum of the aggregate of all acceptances, including obligations for a participation share in such acceptances, authorized for such institution under this paragraph.

"(E) No institution shall accept bills, or be obligated for a participation share in such bills, whether in a foreign or domestic transaction, for any one person, partnership, corporation, association or other entity in an amount equal at any time in the aggregate to more than 10 per centum of its paid up and unimpaired capital stock and surplus, or, in the case of a United States branch or agency of a foreign bank, its dollar equivalent as determined by the Board under subparagraph (H), unless the institution is secured either by attached documents or by some other actual security growing out of the same transaction as the acceptance.

"(F) With respect to an institution which issues an acceptance, the limitations contained in this paragraph shall not apply to that portion of an acceptance which is issued by such institution and which is covered by a participation agreement sold to another institution.

"(G) In order to carry out the purposes of this paragraph, the Board may define any of the terms used in this paragraph, and, with respect to institutions which do not have capital or capital stock, the Board shall define an equivalent measure to which the limitations contained in this paragraph shall apply.

"(H) Any limitation or restriction in this paragraph based on paid-up and unimpaired capital stock and surplus of an institution shall be deemed to refer, with respect to a United States branch or agency of a foreign bank, to the dollar equivalent of the paid-up capital stock and surplus of the foreign bank, as determined by the Board, and if the foreign bank has more than one United States branch or agency, the business transacted by all such branches and agencies shall be aggregated in determining compliance with the limitation or restriction.".

TITLE III—EXPORT TRADE CERTIFICATES OF REVIEW

EXPORT TRADE PROMOTION DUTIES OF SECRETARY OF COMMERCE

C 4011.

SEC. 301. To promote and encourage export trade, the Secretary may issue certificates of review and advise and assist any person with respect to applying for certificates of review.

APPLICATION FOR ISSUANCE OF CERTIFICATE OF REVIEW

C 4012.

SEC. 302. (a) To apply for a certificate of review, a person shall submit to the Secretary a written application which—

(1) specifies conduct limited to export trade, and

(2) is in a form and contains any information, including information pertaining to the overall market in which the applicant operates, required by rule or regulation promulgated under section 310.

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(b)(1) Within ten days after an application submitted under subsection (a) is received by the Secretary, the Secretary shall publish in the Federal Register a notice that announces that an application for a certificate of review has been submitted, identifies each person submitting the application, and describes the conduct for which the application is submitted.

(2) Not later than seven days after an application submitted under subsection (a) is received by the Secretary, the Secretary shall transmit to the Attorney General—

(A) a copy of the application,

(B) any information submitted to the Secretary in connection with the application, and

(C) any other relevant information (as determined by the Secretary) in the possession of the Secretary, including information regarding the market share of the applicant in the line of commerce to which the conduct specified in the application relates.

ISSUANCE OF CERTIFICATE

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SEC. 303. (a) A certificate of review shall be issued to any applicant that establishes that its specified export trade, export trade activities, and methods of operation will—

(1) result in neither a substantial lessening of competition or restraint of trade within the United States nor a substantial restraint of the export trade of any competitor of the applicant,

(2) not unreasonably enhance, stabilize, or depress prices within the United States of the goods, wares, merchandise, or services of the class exported by the applicant,

(3) not constitute unfair methods of competition against competitors engaged in the export of goods, wares, merchandise, or services of the class exported by the applicant, and

(4) not include any act that may reasonably be expected to result in the sale for consumption or resale within the United States of the goods, wares, merchandise, or services exported by the applicant.

(b) Within ninety days after the Secretary receives an application for a certificate of review, the Secretary shall determine whether the applicant's export trade, export trade activities, and methods of operation meet the standards of subsection (a). If the Secretary, with the concurrence of the Attorney General, determines that such standards are met, the Secretary shall issue to the applicant a certificate of review. The certificate of review shall specify—

(1) the export trade, export trade activities, and methods of operation to which the certificate applies,

(2) the person to whom the certificate of review is issued, and

(3) any terms and conditions the Secretary or the Attorney General deems necessary to assure compliance with the standards of subsection (a).

(c) If the applicant indicates a special need for prompt disposition, the Secretary and the Attorney General may expedite action on the application, except that no certificate of review may be issued within thirty days of publication of notice in the Federal Register under section 302(b)(1).

(d)(1) If the Secretary denies in whole or in part an application for a certificate, he shall notify the applicant of his determination and the reasons for it.

(2) An applicant may, within thirty days of receipt of notification that the application has been denied in whole or in part, request the Secretary to reconsider the determination. The Secretary, with the concurrence of the Attorney General, shall notify the applicant of the determination upon reconsideration within thirty days of receipt of the request.

(e) If the Secretary denies an application for the issuance of a certificate of review and thereafter receives from the applicant a request for the return of documents submitted by the applicant in connection with the application for the certificate, the Secretary and the Attorney General shall return to the applicant, not later than thirty days after receipt of the request, the documents and all copies of the documents available to the Secretary and the Attorney General, except to the extent that the information contained in a document has been made available to the public.

(f) A certificate shall be void ab initio with respect to any export trade, export trade activities, or methods of operation for which a certificate was procured by fraud.

REPORTING REQUIREMENT; AMENDMENT OF CERTIFICATE; REVOCATION OF CERTIFICATE

SC 4014.

SEC. 304. (a)(1) Any applicant who receives a certificate of review—

(A) shall promptly report to the Secretary any change relevant to the matters specified in the certificate, and

(B) may submit to the Secretary an application to amend the certificate to reflect the effect of the change on the conduct specified in the certificate.

(2) An application for an amendment to a certificate of review shall be treated as an application for the issuance of a certificate. The effective date of an amendment shall be the date on which the application for the amendment is submitted to the Secretary.

(b)(1) If the Secretary or the Attorney General has reason to believe that the export trade, export trade activities, or methods of operation of a person holding a certificate of review no longer comply with the standards of section 303(a), the Secretary shall request such information from such person as the Secretary or the Attorney General deems necessary to resolve the matter of compliance. Failure to comply with such request shall be grounds for revocation of the certificate under paragraph (2).

(2) If the Secretary or the Attorney General determines that the export trade, export trade activities, or methods of operation of a person holding a certificate no longer comply with the standards of section 303(a), or that such person has failed to comply with a request made under paragraph (1), the Secretary shall give written notice of the determination to such person. The notice shall include a statement of the circumstances underlying, and the reasons in support of, the determination. In the 60-day period beginning 30 days after the notice is given, the Secretary shall revoke the certificate or modify it as the Secretary or the Attorney General deems necessary to cause the certificate to apply only to the export trade, export trade activities, or methods of operation which are in compliance with the standards of section 303(a).

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(3) For purposes of carrying out this subsection, the Attorney General, and the Assistant Attorney General in charge of the antitrust division of the Department of Justice, may conduct investigations in the same manner as the Attorney General and the Assistant Attorney General conduct investigations under section 3 of the Antitrust Civil Process Act, except that no civil investigative demand may be issued to a person to whom a certificate of review is issued if such person is the target of such investigation.

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JUDICIAL REVIEW; ADMISSIBILITY

SEC. 305. (a) If the Secretary grants or denies, in whole or in part, an application for a certificate of review or for an amendment to a certificate, or revokes or modifies a certificate pursuant to section 304(b), any person aggrieved by such determination may, within 30 days of the determination, bring an action in any appropriate district court of the United States to set aside the determination on the ground that such determination is erroneous. 15 USC

(b) Except as provided in subsection (a), no action by the Secretary or the Attorney General pursuant to this title shall be subject to judicial review.

(c) If the Secretary denies, in whole or in part, an application for a certificate of review or for an amendment to a certificate, or revokes or amends a certificate, neither the negative determination nor the statement of reasons therefor shall be admissible in evidence, in any administrative or judicial proceeding, in support of any claim under the antitrust laws.

PROTECTION CONFERRED BY CERTIFICATE OF REVIEW

SEC. 306. (a) Except as provided in subsection (b), no criminal or civil action may be brought under the antitrust laws against a person to whom a certificate of review is issued which is based on conduct which is specified in, and complies with the terms of, a certificate issued under section 303 which certificate was in effect when the conduct occurred. 15 USC

(b)(1) Any person who has been injured as a result of conduct engaged in under a certificate of review may bring a civil action for injunctive relief, actual damages, the loss of interest on actual damages, and the cost of suit (including a reasonable attorney's fee) for the failure to comply with the standards of section 303(a). Any action commenced under this title shall proceed as if it were an action commenced under section 4 or section 16 of the Clayton Act, except that the standards of section 303(a) of this title and the remedies provided in this paragraph shall be the exclusive standards and remedies applicable to such action. 15 USC

(2) Any action brought under paragraph (1) shall be filed within two years of the date the plaintiff has notice of the failure to comply with the standards of section 303(a) but in any event within four years after the cause of action accrues.

(3) In any action brought under paragraph (1), there shall be a presumption that conduct which is specified in and complies with a certificate of review does comply with the standards of section 303(a).

(4) In any action brought under paragraph (1), if the court finds that the conduct does comply with the standards of section 303(a), the court shall award to the person against whom the claim is brought the cost of suit attributable to defending against the claim (including a reasonable attorney's fee).

(5) The Attorney General may file suit pursuant to section 15 of the Clayton Act (15 U.S.C. 25) to enjoin conduct threatening clear and irreparable harm to the national interest.

GUIDELINES

SC 4017.

SEC. 307. (a) To promote greater certainty regarding the application of the antitrust laws to export trade, the Secretary, with the concurrence of the Attorney General, may issue guidelines—

(1) describing specific types of conduct with respect to which the Secretary, with the concurrence of the Attorney General, has made or would make, determinations under sections 303 and 304, and

(2) summarizing the factual and legal bases in support of the determinations.

(b) Section 553 of title 5, United States Code, shall not apply to the issuance of guidelines under subsection (a).

ANNUAL REPORTS

C 4018.

SEC. 308. Every person to whom a certificate of review is issued shall submit to the Secretary an annual report, in such form and at such time as the Secretary may require, that updates where necessary the information required by section 302(a).

DISCLOSURE OF INFORMATION

C 4019.

SEC. 309. (a) Information submitted by any person in connection with the issuance, amendment, or revocation of a certificate of review shall be exempt from disclosure under section 552 of title 5, United States Code.

(b)(1) Except as provided in paragraph (2), no officer or employee of the United States shall disclose commercial or financial information submitted in connection with the issuance, amendment, or revocation of a certificate of review if the information is privileged or confidential and if disclosure of the information would cause harm to the person who submitted the information.

(2) Paragraph (1) shall not apply with respect to information disclosed—

(A) upon a request made by the Congress or any committee of the Congress,

(B) in a judicial or administrative proceeding, subject to appropriate protective orders,

(C) with the consent of the person who submitted the information,

(D) in the course of making a determination with respect to the issuance, amendment, or revocation of a certificate of review, if the Secretary deems disclosure of the information to be necessary in connection with making the determination,

(E) in accordance with any requirement imposed by a statute of the United States, or

(F) in accordance with any rule or regulation promulgated under section 310 permitting the disclosure of the information to an agency of the United States or of a State on the condition that the agency will disclose the information only under the circumstances specified in subparagraphs (A) through (E).

RULES AND REGULATIONS

SEC. 310. The Secretary, with the concurrence of the Attorney General, shall promulgate such rules and regulations as are necessary to carry out the purposes of this Act. 15 U

DEFINITIONS

SEC. 311. As used in this title— 15 U

(1) the term "export trade" means trade or commerce in goods, wares, merchandise, or services exported, or in the course of being exported, from the United States or any territory thereof to any foreign nation,

(2) the term "service" means intangible economic output, including, but not limited to—

(A) business, repair, and amusement services,

(B) management, legal, engineering, architectural, and other professional services, and

(C) financial, insurance, transportation, informational and any other data-based services, and communication services,

(3) the term "export trade activities" means activities or agreements in the course of export trade,

(4) the term "methods of operation" means any method by which a person conducts or proposes to conduct export trade,

(5) the term "person" means an individual who is a resident of the United States; a partnership that is created under and exists pursuant to the laws of any State or of the United States; a State or local government entity; a corporation, whether organized as a profit or nonprofit corporation, that is created under and exists pursuant to the laws of any State or of the United States; or any association or combination, by contract or other arrangement, between or among such persons,

(6) the term "antitrust laws" means the antitrust laws, as such term is defined in the first section of the Clayton Act (15 U.S.C. 12), and section 5 of the Federal Trade Commission Act (15 U.S.C 45) (to the extent that section 5 prohibits unfair methods of competition), and any State antitrust or unfair competition law,

(7) the term "Secretary" means the Secretary of Commerce or his designee, and

(8) the term "Attorney General" means the Attorney General of the United States or his designee.

EFFECTIVE DATES

SEC. 312. (a) Except as provided in subsection (b), this title shall take effect on the date of the enactment of this Act. 15 U note.

(b) Section 302 and section 303 shall take effect 90 days after the effective date of the rules and regulations first promulgated under section 310.

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TITLE IV—FOREIGN TRADE ANTITRUST IMPROVEMENTS

SHORT TITLE

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SEC. 401. This title may be cited as the "Foreign Trade Antitrust Improvements Act of 1982".

AMENDMENT TO SHERMAN ACT

SEC. 402. The Sherman Act (15 U.S.C. 1 et seq.) is amended by inserting after section 6 the following new section:

USC 6a.

"SEC. 7. This Act shall not apply to conduct involving trade or commerce (other than import trade or import commerce) with foreign nations unless—

"(1) such conduct has a direct, substantial, and reasonably foreseeable effect—

"(A) on trade or commerce which is not trade or commerce with foreign nations, or on import trade or import commerce with foreign nations; or

"(B) on export trade or export commerce with foreign nations, of a person engaged in such trade or commerce in the United States; and

"(2) such effect gives rise to a claim under the provisions of this Act, other than this section.

If this Act applies to such conduct only because of the operation of paragraph (1)(B), then this Act shall apply to such conduct only for injury to export business in the United States.".

AMENDMENT TO FEDERAL TRADE COMMISSION ACT

SEC. 403. Section 5(a) of the Federal Trade Commission Act (15 U.S.C. 45(a)) is amended by adding at the end thereof the following new paragraph:

"(3) This subsection shall not apply to unfair methods of competition involving commerce with foreign nations (other than import commerce) unless—

"(A) such methods of competition have a direct, substantial, and reasonably foreseeable effect—

"(i) on commerce which is not commerce with foreign nations, or on import commerce with foreign nations; or

"(ii) on export commerce with foreign nations, of a person engaged in such commerce in the United States; and

"(B) such effect gives rise to a claim under the provisions of this subsection, other than this paragraph.

If this subsection applies to such methods of competition only because of the operation of subparagraph (A)(ii), this subsection shall apply to such conduct only for injury to export business in the United States.".

Approved October 8, 1982.

LEGISLATIVE HISTORY—S. 734 (H.R. 1799, H.R. 6016):

HOUSE REPORTS: No. 97-924 (Comm. of Conference), No. 97-637, pt. 1 accompanying H.R. 1799 (Comm. on Foreign Affairs), pt. 2 (Comm. on the Judiciary) and No. 97-629 accompanying H.R. 6016 (Comm. on Banking, Finance and Urban Affairs).

SENATE REPORTS: No. 97-27 (Comm. on Banking, Housing and Urban Affairs) and No. 97-644 (Comm. of Conference).

CONGRESSIONAL RECORD:

Vol. 127 (1981): Apr. 7, 8, considered and passed Senate.

Vol. 128 (1982): July 27, H.R. 1799 and H.R. 6016 considered and passed House; S. 734, amended, passed in lieu.

Oct. 1, Senate and House agreed to conference report.

WEEKLY COMPILATION OF PRESIDENTIAL DOCUMENTS:

Vol. 18, No. 41 (1982): Oct. 8, Presidential statement.

Appendix 2.—Commerce, Consumer, and Monetary Affairs Subcommittee's May 9, 1986, Staff Report of Telephone Conversations With ETC Officials

HOUSE OF REPRESENTATIVES
COMMERCE, CONSUMER, AND MONETARY AFFAIRS SUBCOMMITTEE STAFF REPORT ON TELEPHONE CONVERSATIONS WITH EXPORT TRADING COMPANIES

May 9, 1986

A. Background

Prior the to the Subcommittee's March 4, 1986, hearing on the impact and implementation of the Export Trading Company Act, I contacted by telephone numerous export trading companies (ETCs), some of whom had been contacted by GAO in connection with its examination and report. Subsequent to the hearing, I contacted additional ETCs, ones which the Export Import Bank had indicated were recipients of a loan guarantee under the Ex-Im Bank's Working Capital Guarantee Program for both exporters and ETCs. The following accurately reflects what ETC officials advised me of their operations, suggestions for improvement, and problems with the implementation of the ETC Act.

B. ETCs/Exporter Recipients of Ex-Im Loan Guarantees

I contacted 13 ETCs and exporters listed by Ex-Im as receiving Ex-Im loan guarantees. Three of the 13 refused to call back after 2 or more telephone calls, but I did talk over the telephone with 10 of the ETC/exporter officials, (although one did have some suggestions for improvement, but never had the time to elaborate on them.)

Interestingly, 5 of the 10 persons I interviewed advised me that they had not accepted the Ex-Im Guarantee, had not paid 1 to 1.5 percent guarantee fee necessary to finalize it, because of problems with the program or the conditions surrounding the loan guarantee. (This is in addition to ETC Hearing witness Howard Hammonds who is listed as a recipient, but who could not draw down upon the loan, and also one recipient listed for a joint Ex-Im/SBA loan guarantee, but which cancelled it.) Three of this group who are listed as recipients, but who are not, have submitted letters for the record, which are contained elsewhere in the Appendix to the March 4th Hearing Transcript, and therefore I have not included their comments in this report. With one minor exception, this report reflects only the results of my telephone survey.

Two of the listed recipients had no problems with the program. One of the two is "very happy with the program," which involved a $1 million machinery and architectural and engineering contract, receiving the guarantee in early 1985. Another recipient was happy with the program and obtained the loan guarantee approval in two months. (However, he was listed as receiving two guarantees and he has only received one.) He said that he was "happy; everything is going smoothly."

Three other persons listed as recipients were not as satisfied. One ETC complained about the Ex-Im requirement for a personal guarantee, an unusual financial requirement for a corporation. Ex -Im also wanted as collateral, his personal home, but he absolutely refused on that. There was much too much paperwork and it was burdensome. Because of the personal guarantee requirement, he declined the guarantee offered by Ex-Im in late 1984 and was able to find financing without the guarantee. He suggested more widespread export subsidies, and indicated that much time and effort is spent trying to find and individualize financing for a particular business. In any event, exporters need capital, not additional debt.

Another ETC official which accepted the guarantee confronted a number of problems. He, too, was bothered by Ex-Im's requirement that he and others personally "jointly and severally" guarantee the loan. The bank processing this for him, his ETC's regular bank, had a lot of difficulty, and had to continually ask him a lot of questions because Ex-Im had additional questions. The administrative requirements were burdensome. For example, Ex-Im wanted an approved invoice for every transaction covered by the working capital loan, an unusual practice. He felt that Ex-Im Bank "didn't have the foggiest notion of what they wanted," and that, consequently, it took 9 months to get the guarantee, finally approved in mid-1985. Often, Ex-Im staff working on this loan were not in their office. It was a difficult experience.

Finally, a third ETC's senior official complained about the lengthy delays, the administrative burden, and the requirement for a personal guarantee, which is not a usual lender requirement—his firm declined the guarantee because of the personal guarantee requirement. (This person is generally familiar with, not only his own firm's experience but also other firm's experiences as well.)

C. Experiences of other ETCs with the 1982 Act's Implementation and their Problems

A senior official of a regional bank ETC in the Mid-Atlantic Region advised me of the following:

> --Regional banks believe that ETCs will service the bank customers, but it often does not work out that way. To be successful, ETC must focus narrowly on particular products or services, developing personal relationships with foreign distributors and buyers and ultimately a niche for themselves. Often this means acting as an ETC for only 3 or 4 companies; in his case, he is handling international marketing of products for small manufacturing companies. Specialization and establishing the overseas trading network relationships are the keys to success.
>
> —Also, banks must expect red ink in the first few years, as it takes that long to prove to foreigners that you are reliable and can do the business.
>
> —Even a bank ETC is confronted with the same problem that non-bank ETCs face: coming up with the financing. Often his parent bank wants $1 million plus deals; they don't want the small deals. (Another ETC advised me independently that it had tried to obtain financing from this particular bank, but was rejected for that reason.) This official told me that, "What is lacking is a mechanism to help financially support a smaller level of deals."
>
> —Their problems with the Federal Reserve Regulations are more narrowly focused than those of the money center banks: Their big concern is the 51 percent test. He is very worried about that. His ETC has been importing from Latin America, which needs its exports to generate enough revenue in order to be able to import from the United States. In other words, the ETC must import to enable foreign countries to earn enough revenues for U.S. exports. The Federal Reserve Board does not recognize this.

Another Mid-Atlantic bank ETC official told me that a successful ETC must (1) hire experienced people, preferably traders, (2) utilize joint ventures for this purpose, possibly with experienced traders/trading companies—his firm is considering a joint venture with a European trading company, and (3) focus on certain products, in his case,, agricultural commodities and certain general merchandise. Trading is so "countercultural" to banking, that traders must be involved; placing bankers in charge of the ETC does not work.

An official of a bank ETC located in the West told me that his firm had retrenched and was focusing on two product areas (medical goods and food), not on others as it had done in the past. Finding good distribution networks abroad is what makes an ETC successful. The start-up costs for this ETC were enormous—the interviewee implied that their enormity had been unexpected—and there had been much sorting out. The parent bank had been very helpful in referring potential clients to the ETC. Financing was a problem, but the interviewee did not elaborate.

A non-bank ETC president in the New York metropolitan area told me of his ETC's experience. His firm trades for apparel and textile manufacturers, primarily buying textiles for export. He cited the following problems:

—Certification under the 1982 Act required much paperwork and resulted in a 6 month delay. He recommended streamlining the process.

—Financing is still the greatest problem; banks are not really as interested because export financing is not as profitable and involves small deals; banks want a proven "track record". For example, he needs a long term loan facility, such as "$10 million for 10 years". "Money buys the staying power", because often the ETC is operating 2 to 3 years before it succeeds.

—Also, ETCs need additional information and accounting, legal, and managerial assistance; there needs to be a special program for them, perhaps with the Commerce Department helping. (My thought: this might be similar to the SBA's management assistance program and its SCORE small business counseling.)

A non-bank ETC in the Washington, D. C., area is involving primarily with high technology equipment. In the opinion of one of its officers,

—"The problem with the Act is money. And the financing which is missing is venture capital, funds to do market development and to pay salaries and overhead in the early years." He is annoyed that the SBA will provide loan assistance to an "Italian restaurant on K Street in downtown Washington, D.C.," but it is extremely hard to obtain Federal financial assistance (loans or guarantees) for exporting, although "that is more important for us as a nation."

—The Commerce Department certificate is not of much benefit, and they could do without it.

—The Commerce Department could "look more favorable on market development", once the ETC is in business.

A New York area ETC official told me that "we are shooting ourself in the leg by looking for quick results." The most successful ETCs are those with lowered expectations. He does not believe that certification has been that helpful. There needs to be more of an incubator role for ETCs as they begin operations. The problem is financing, and the need for blended Ex-Im rates.

D. Conclusions

For the most part, what I found out from these ETC officials confirmed what the General Accounting Office found and what witnesses testified to during our March 4th hearing. New and additional facts, points, and suggestions came to light, however, and are set forth above.

S. McSpadden
Stephen R. McSpadden
Subcommittee Staff Counsel

APPENDIX 3.—1985 REPORT BY THE OFFICE OF INSPECTOR GENERAL, COMMERCE DEPARTMENT, "IMPLEMENTATION OF THE EXPORT TRADING COMPANY PROGRAM: I.T.A."

IMPLEMENTATION OF THE
EXPORT TRADING COMPANY PROGRAM

INTERNATIONAL TRADE ADMINISTRATION

2-152-5-004

UNITED STATES DEPARTMENT OF COMMERCE

OFFICE OF INSPECTOR GENERAL

JULY 1985

UNITED STATES DEPARTMENT OF COMMERCE
Office of Inspector General
Washington, D.C. 20230

JUL 17 1985

MEMORANDUM FOR: Kenn George
Acting Under Secretary
for International Trade

FROM: John R. Szpanka John Szpanka
Assistant Inspector General
for Auditing

SUBJECT: Implementation of the Export
Trading Company Program
Audit Report No. 2-152-5-004

Attached is the final report on our audit of activities undertaken by the International Trade Administration (ITA) to implement the Export Trading Company Act of 1982. An Executive Summary of the audit findings begins on page i. Incorporated in this final report is a complete copy of ITA's response to our draft report.

Our specific recommendations are shown on page 10. As required by Department Administrative Order 213-5, please provide us within 90 days an action plan for each of our recommendations.

We appreciate the cooperation and courtesies extended by ITA officials during our audit.

Attachment

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IMPLEMENTATION OF THE EXPORT TRADING COMPANY PROGRAM

EXECUTIVE SUMMARY

The Export Trading Company Act of 1982 (Act) was designed to help increase U.S. exports. Enactment of this legislation was expected to stimulate the creation of hundreds of thousands of trade-related jobs. Specifically, the Act:

1. Directed the Department of Commerce to establish an office to promote and encourage the formation of export trading companies (ETCs). Title I of the Act basically defines an ETC as a profit or nonprofit organization which is organized and operated principally for purposes of:

   -- Exporting goods or services produced in the United States; or

   -- Facilitating the exportation of goods or services produced in the United States by unaffiliated persons by providing one or more export trade services, such as advertising, marketing, insurance, transportation, etc.

2. Allowed certain banking institutions to invest in ETCs.

3. Strengthened specific areas of export financing.

4. Authorized the Secretary of Commerce, with the Attorney General's concurrence, to issue certificates of review providing limited antitrust immunity for certain export trade conduct. Certificates are available not just to ETCs but to any person engaged in export trade.

5. Clarified the jurisdictional reach of the antitrust laws with respect to export trade.

Our report focuses principally on those portions of the Act which the Department of Commerce's International Trade Administration (ITA) is responsible for administering; see items 1 and 4 above. Specific issues are briefly summarized below:

o ITA's Office of Export Trading Company Affairs (OETCA) was created in response to the Act's requirement to establish an office to promote and encourage the formation of ETCs. The Act specifies that the office is to promote and encourage the formation of ETCs by providing (1) information and advice to interested persons and (2) a referral service to facilitate contact between producers of exportable goods and services and the various firms offering export trade services.

OETCA has undertaken an active role in informing the business community about the Act and, during this process, has relied heavily on ITA's network of 47 district offices to help interact with business firms to stimulate an interest in ETCs. Trade specialists in the district offices participated in an initial round of ETC awareness seminars during calendar year 1983 but, since then, ETC activity has sharply declined in these offices. (See page 4.) Under these conditions, little work is now being done by the trade specialists to assist OETCA in promoting and encouraging the formation of ETCs. District office personnel need current guidance to know what additional efforts, if any, should be expended on the ETC program. In response to our draft report, ITA basically agreed with our recommendations on this subject.

o We obtained some information about the progress made toward implementing the Act's provisions relating to a strengthened financial position for the ETCs. Our review did not focus on this area because the Federal Reserve Board and the Export-Import Bank have direct management responsibility over this part of the Act. Basic observations are:

  -- An important objective of the Act was to provide for infusions of ETC equity capital through investments made by bank holding companies. There are approximately 5,000 bank holding companies but as of September 30, 1984, only 29 of these firms had taken formal action to make ETC investments. Included in these 29 firms, however, were a number of the Nation's largest banking institutions. (See page 12.)

  -- The Act directs the Export-Import Bank to establish a loan guarantee program for ETCs and other exporters. Relatively few of these loan guarantees had been made at the time of our review, although some recent actions have been taken to improve this condition. (See page 14.)

o Thousands of firms have been represented at seminars describing the advantages of the Act. However, at the close of FY 1984, only 63 organizations had sought the antitrust protection conferred by certificates of review authorized under Title III of the Act. Most of the firms that we visited had not applied for a certificate because they did not anticipate a need for such antitrust protection. In this regard, however, ITA officials believe there will be an increased level of certificate applications as the overall export environment improves. (See page 17.)

o Regarding the processing of applications for certificates of review, OETCA has established a systematic approach for controlling and reviewing each incoming case. Working closely with the Office of General Counsel, OETCA has processed the applications in a thorough and timely manner. (See page 20.)

Has the Act been successful in generating large amounts of new exports? ITA does not have a data base to begin addressing this question on a comprehensive basis. For instance, there are unknown thousands of ETCs, as defined by the Act. No mechanism exists to identify these organizations, gauge how many new ETCs have been formed, or ascertain the amount of increased export sales generated by ETC activity. Organizations receiving certificates of review are required to provide ITA with an annual report showing export sales data and other information, but there is no established way of estimating what portion of these reported sales occurred as a result of the certificates.

Data obtained during our review indicates that progress of the ETC program has been slow in stimulating additional exports. A number of individuals pointed out that the development of the ETC network is still at a relatively early stage and that it will take more time before substantial progress is made. For example, the Japanese took many years to establish a solid ETC structure.

INTRODUCTION

The Office of Audits, Office of Inspector General, has completed an audit of activities undertaken by the International Trade Administration (ITA) to implement the Export Trading Company Act of 1982 (Act). The audit was made under the authority of the Inspector General Act of 1978 and Department Organization Order 10-13, dated May 22, 1980.

Purpose And Scope

The purpose of our audit was to evaluate the approaches being used by ITA to:

- Promote and encourage the formation of Export Trading Companies (ETCs).
- Process and review applications for the antitrust protection conferred by certificates of review.

Our audit focused on the ETC activities administered by ITA's (1) Office of Export Trading Company Affairs (OETCA) and (2) district offices in Chicago, Illinois; Dallas, Texas; New York, New York; and San Francisco, California. Our coverage included interviews with personnel in the Office of the General Counsel. We also met with officials at the Department of Justice, Federal Reserve Board, and the Export-Import Bank (Eximbank) to obtain information about the ETC activities being administered by their organizations. In addition, we interviewed representatives of 37 ETCs and other private sector firms, including banking institutions, located across the country.

The audit was conducted in accordance with generally accepted Government auditing standards.

Background

On October 8, 1982, the President signed the Act (Public Law 97-290). In developing this legislation, Congress recognized that our economy depends heavily on exports. Essentially, the Act was designed to create new ways for the private sector to improve its ability to compete in the international marketplace. It was anticipated that this legislation would help create hundreds of thousands of new trade-related U.S.

jobs in the near future. Outlined below are the principal features of the Act's four titles:

- Title I basically defines an ETC as a profit or nonprofit organization which is organized and operated principally for purposes of:
  - Exporting goods or services produced in the United States; or
  - Facilitating the exportation of goods or services produced in the United States by unaffiliated persons by providing one or more export trade services, such as advertising, marketing, insurance, transportation, etc. Thousands of small and medium-sized firms produce goods and services that are competitive overseas, but the firms are inhibited from exporting by their unfamiliarity with foreign markets, customs and laws. Individually, they can't afford the costs and risks to develop the necessary expertise to penetrate those markets. ETCs can provide firms with the export services needed to do this. Through specialization, cost dispersion and economies of scale, ETCs can serve as ideal intermediaries to facilitate the exports of these companies.

  This title directs the Department of Commerce to establish an office to promote and encourage the formation of ETCs by providing (1) information and advice to interested persons and (2) a referral service to facilitate contact between producers of exportable goods and services and firms offering export trade services. OETCA was created in response to these requirements. With a staff of 17 people, OETCA has performed various activities designed to further the intent of the Act, including:

  - Initiating ETC-related conferences and presentations throughout the country.
  - Counseling business representatives about the Act's provisions.
  - Initiating the contact referral service required by the Act.
  - Processing and evaluating applications for export trade certificates of review.

- Title II permits bank holding companies and other specified banking entities to invest in ETCs, establishes a program for loan guarantees by the Eximbank and amends the Federal Reserve Act by removing certain restrictions on the use of bankers' acceptances.

- Title III provides for the issuance of export trade certificates of review by the Department of Commerce (with the concurrence of the Department of Justice) under which export conduct may receive specific antitrust protection. Certificates are available not just to ETCs but to any "person" engaged in export trade. The definition of "person" covers a broad range of entities -- individuals, partnerships, corporations, joint ventures, and local government entities. For example, under the definition of "person," a single U.S. company may apply for a certificate even though its export trade is only a small part of its overall business operations.

- Title IV clarifies the jurisdictional reach of the Sherman Act and the Federal Trade Commission Act with respect to export-related commerce.

ITA FIELD PERSONNEL NEED CURRENT GUIDANCE REGARDING ETC ACTIVITIES

OETCA has undertaken an active role in notifying the business community about the Act and, during this process, has relied heavily on ITA's network of 47 district offices to help interact with the business community and stimulate an interest in ETCs. Trade specialists in the district offices participated in an initial round of ETC awareness seminars during calendar year 1983 but, since then, ETC activity has sharply declined in these offices. For instance, at the four offices we visited, trade specialists were discussing the ETC program very infrequently during counseling sessions with business firms.

In this regard, U.S. and Foreign Commercial Service (US&FCS) managers at ITA headquarters have not established current performance expectations and reporting requirements applicable to ETC activities undertaken by district office personnel. Under these conditions, little work is now being done by the trade specialists to assist OETCA in promoting and encouraging the formation of ETCs. We believe district office personnel need current guidance from ITA headquarters to know what additional efforts, if any, should be expended in assisting OETCA to promote the ETC program.

Publicizing the ETC Act

After the ETC legislation was enacted, OETCA and the district offices arranged for ETC awareness seminars to be held across the Nation to alert business representatives to the provisions of this Act. A total of 49 seminars were held during calendar year 1983. Overall attendance totaled about 12,000 persons, or about 250 per meeting. In preparing for these sessions, district office personnel performed a key role in contacting business representatives and encouraging them to attend. During the seminars, members of the business community received ETC-related information presented by representatives from OETCA, other ITA headquarters offices, the Office of General Counsel and the district offices. During calendar year 1984, OETCA planned to co-sponsor, with certain public accounting firms, a number of additional seminars pertaining to the ETC program. By the end of FY 1984, nine of the planned seminars had been held and six cancelled for lack of interest. Average attendance has totaled 70 persons per seminar. District office personnel performed a minor role in preparing for these meetings. Essentially, they provided the co-sponsors with the names and addresses of potential attendees, to be used in developing mailing lists to announce the seminars.

In addition to seminars, the ETC program was brought to the attention of the business community through speeches by ITA personnel and information contained in various publications. For example, several articles focusing on ETCs appeared in Commerce's magazine of international trade, "Business America." A number of private sector publications also contained such articles. "The Export Trading Company Guidebook" was prepared for ITA by Price Waterhouse and the Council for Export Trading Companies. This 135-page document provides essential information on the functions and advantages of establishing or using an ETC. The Guidebook received widespread distribution in the business community.

Guidelines for District Office Counseling Regarding the ETC Act

On June 2, 1983, US&FCS issued Operations Bulletin No. 83-75 to provide the district offices with guidelines for counseling under the ETC Act. Included in this Bulletin were the following comments.

> "The high level of interest in the formation and operation of ETCs generated through our successful Regional Conferences should be maintained and carried through into current efforts to render appropriate counseling services. Field counseling activities and additional conferences which address a more sophisticated level of interest in the development of ETCs are the next progressive steps in program development preparatory to the receipt of applications for Export Trade Certificates of Review. Your effective administration of field counseling services will be a major contribution to the successful development of the ETC program through the Office of Export Trading Company Affairs (OETCA).

* * * * * *

> "Title I of the ETC Act requires the Commerce Department to provide two counseling services: (1) 'provide information and advice to interested persons' and (2) 'facilitate contact between producers of exportable goods and services and firms offering export trade services.' The District Offices should provide this counseling to any interested individuals or organizations -- not just those interested in bank affiliation or antitrust certification. In providing the first type of counseling service, the District Offices should identify the scope of interest, provide the OETCA information kit, outline the act briefly and answer questions to the extent feasible.... The second type of service will be provided through the Contact Facilitation Service....

> "...The District Offices should explain (1) the mechanics of how to receive detailed counseling in Washington, D.C., (2) how to apply for a Title III certificate and (3) the types of information required by the regulations.... However, due to the complexities of antitrust law, the District Office should only provide general guidance on Title III and not provide specific counseling which could be construed as an opinion. No view as to whether a certificate is needed or what would or would not be certifiable should be offered...."

We inquired about the nature and extent of counseling efforts being undertaken by the district offices after the above described Bulletin was issued. In this regard, the FY 1984 annual planning guidance which US&FCS headquarters provided to the district offices did not mention the ETC program. Likewise, the FY 1984 annual work plans developed by the district offices we visited did not refer to this subject. US&FCS officials advised that no information is available at headquarters to gauge the level of effort being devoted to ETC activities by district office personnel.

Limited Extent of ETC Counseling by District Offices

We visited four district offices to obtain direct information about the extent of ETC activities being undertaken by trade specialists in these offices. Essentially, we found that very little ETC-related work was being performed at these locations.

To help determine the extent of ETC counseling activities being performed at the four offices, we reviewed selected Business Contact Reports (Form ITA-700s) prepared during fiscal year 1984. These forms are prepared by each trade specialist after completing a business counseling session and are designed to identify the kinds of counseling or service rendered. Only 64 of the 4,151 Business Contact Reports we reviewed (1.5 percent) contained any reference to the ETC program. We interviewed 24 trade specialists in the four district offices, and they acknowledged that ETC-related information is discussed very infrequently during the counseling sessions.

Regarding Title III certificates of review, we found only one instance, at the four district offices we visited, where trade specialists had referred potential applicants to OETCA for counseling and assistance. An OETCA official confirmed that, overall, the 47 district offices had referred few potential applicants.

We inquired about the reasons for the lack of fiscal year 1984 ETC activity among the trade specialists. In essence, they informed us that, after the large-scale effort to publicize the ETC program in 1983, the business community had expressed very little enthusiasm or interest in this program. Specifically, many trade specialists found that business firms simply felt there would be little or no benefit from the Act unless a firm had an antitrust problem or banks began making more loan funds available to ETCs. As an example of the lack of interest in the ETC program, we found that a trade specialist at one of the largest district offices was designated in February 1984 as the ETC coordinator for that office but had received only three ETC-related inquiries since that time.

District office personnel advised that they have numerous export expansion programs for delivery to the business community, and the ETC program is only one of these programs. Due to the business community's limited interest in the ETC program, trade specialists have not placed a high priority on this activity.

A number of trade specialists pointed out that they had not received training relating to the ETC program but felt that appropriate training on this subject was needed. Of particular concern was the need for specific information about the various ways in which ETCs can help provide for increased exports. We agree that specific examples would be very helpful in discussions with business representatives.

In summary, most trade specialists at the district offices we visited were doing very little to aid OETCA with the ETC program. Many of these personnel simply do not believe that much effort in this area is warranted, in view of the business community's limited response to the ETC program. We believe it is important for ITA headquarters to provide the district offices with guidance on this subject so that they will know what additional efforts, if any, should be expended in assisting OETCA to promote the ETC program.

Contact Facilitation Service

As previously mentioned, the Act requires the Department to provide a referral service to facilitate contact between (1) producers of exportable goods and services and (2) firms offering export trade services. In response to this requirement, OETCA established the Contact Facilitation Service (CFS). The CFS program was designed to provide a way of registering, in a computerized file, the names and addresses of ETCs or other firms which provide export services and U.S. firms interested in contacting or being contacted by a provider of these services. In essence, this computerized approach provided a convenient way for the firms which were registered in the system to identify and contact each other.

District office personnel provided CFS registration forms to business representatives who expressed an interest in this service. After the forms were completed, district office personnel forwarded them to ITA headquarters for computer input.

Registration of Firms -- At the end of FY 1983, ITA had registered about 1,600 firm names in the CFS computerized files. District office personnel advised that a major portion of these registrations stemmed from the large number of attendees at the 1983 ETC seminars. By the end of FY 1984, however, the number of entries registered in the CFS increased by only 200 firms. Of the approximately 1,800 names included in CFS at that time, we found that many were duplicates. So, the actual number of individual firms was significantly less than 1,800.

Relatively few of the thousands of ETCs are registered in the CFS file. For example, our randomly selected list of 100 ETCs revealed that only one of these firms was included in the file. Most of the ETCs that we visited were not aware of the CFS and had never been approached by district office personnel to discuss this listing.

Usage of CFS Data -- Initially, ITA charged a $25 fee to firms which registered in the computerized file. Registered firms were entitled to obtain, for an additional $25 fee, a search of the computerized file to identify other companies which matched specified product lines of interest. Firms requesting a search were also charged $5 for each company name actually identified as a result of the computer search. Soon after the registration process began, ITA modified the fee structure so that the $25 registration fee was eliminated, but the computerized search fee was increased to $50. No change was made to the $5 fee for each company name identified during the computer search.

Business community representatives made little use of the computerized CFS files. ITA representatives estimate that, since the inception of the computerized matching system, less than a dozen inquiries were received.

Recognizing that the CFS computerized matching service did not achieve its intended purpose, OETCA concluded that the lack of such activity was the result of fees being assessed for this service. Accordingly, OETCA discontinued the computerized search service, and in lieu thereof, began in June 1984, distributing without charge a CFS directory. This document identified all the firms registered in the CFS system, including producers of exportable goods and services as well as ETCs and other export intermediaries. With this directory, registrants and others can identify and contact each other with a view to developing mutually agreeable exporting arrangements. OETCA is relying primarily on the district offices to distribute the directory. To keep the directory current, OETCA intends to update the contents on a periodic basis.

Reasons for Lack of Use of CFS Data -- Some of the exporting firms said they would prefer to have personal knowledge of an ETC organization, rather than relying on a listing of firms. Also, during our visits to various district offices, we learned that many of the trade specialists have a poor regard for CFS information. For instance, trade specialists are quite concerned that their credibility with client firms will be seriously damaged if the clients rely on the CFS listing and select an ETC organization which does a poor job.

Trade specialists told us that they are concerned because any ETC organization, without regard to qualifications, can register for inclusion on the CFS listing. In this regard, however, we found that instructions provided to the district offices specified that these offices were to screen CFS registrants to ensure that a service firm has the experience and expertise to provide the services offered. (Most trade specialists that we interviewed were not aware of this instruction.) There was no further guidance from ITA headquarters regarding the approach to be used in determining whether a service firm has the necessary experience and expertise to qualify for CFS registration.

Results of Legislation

Has the Act been successful in generating large amounts of new exports? ITA does not have a data base to begin addressing this question on a comprehensive basis. For instance, there are unknown thousands of ETCs, as defined by the Act. No mechanism exists to identify these organizations, gauge how many new ETCs have been formed, or ascertain the amount of increased export sales generated by ETC activity. Organizations receiving certificates of review under Title III are required to provide ITA with an annual report showing export sales data and other information, but there is no established way of estimating what portion of these reported sales occurred as a result of the certificates. (See page 20.)

Although there is an overall lack of quantitative data regarding export results under the ETC program, the information obtained during our review nevertheless indicates that progress has been slow. Several of the people that we interviewed pointed out that the development of the ETC network is still at a relatively early stage and that it will take more time before substantial progress is made. They advised that the Japanese took many years to establish a solid ETC structure. Also, an ITA official pointed out that passage of the legislation coincided with the advent of a number of external events which seriously impaired the ability of U.S. firms to compete effectively in export markets; i.e., a strong dollar, a debt crisis in developing nations, and the illiquidity of several foreign currencies.

RECOMMENDATIONS

We recommended that the Under Secretary for International Trade take the necessary actions to:

1. Ensure that personnel in the district offices receive current information as to what they are expected to do in helping OETCA to promote and encourage the formation of ETCs. Also, provide for a clear understanding regarding the level of district office effort to be expended on ETC matters and the kind of performance reporting to be submitted relating to these activities.

2. Provide district office personnel with appropriate training relating to ETC program matters.

3. Reassess the CFS listing to determine whether improvements can be made to increase the confidence level of business representatives in the usefulness of this listing.

AGENCY COMMENTS

In responding to our draft report, ITA basically agreed with the recommendations and advised that:

Recommendation No. 1

"A new Operations Bulletin will be issued (updating O.B. 83-75) to provide current information on what the role of district offices will be promoting and encouraging the formation of ETCs. Included will be a clarification of the respective roles to be played by OETCA and the field. In addition, guidelines and procedures will be included on how the US&FCS/Federal Bar Association agreement can be utilized to provide ETC legal counseling to business firms.

"A series of nine regional seminars on ETC will be planned during FY/86 (beginning in October 1985). The program and agenda will be prepared jointly by OETCA and US&FCS.

"The Management Planning Guidelines for Domestic Operations will be amended to specify that, among the mix of marketing strategies, an ETC component will be included when planning for the delivery of counseling services. This action will have the effect of measuring such efforts (under Critical Element II) against annual performance appraisals for Directors and other field personnel.

"The Business Counseling form ... used by trade specialists in reporting counseling sessions and actions, has been revised to include ETC data by type of account and export results reported. District office briefing reports will also include ETC activity when appropriate."

Recommendation No. 2

"We fully endorse this recommendation.... [US&FCS] will cooperatively work with OETCA in developing a training program that meets the specific needs of district office trade specialists."

Recommendation No. 3

"We are in general agreement on what the report says on the reception CFS has received from both business firms and the district offices. Some improvements are called for on both the criteria for registering firms on the CFS and the marketing of CFS.... [OETCA will] provide improved guidelines which will be issued to the field in the Operations Bulletin mentioned above."

STIMULATING ETC EQUITY INVESTMENTS AND LOAN FINANCING

Recognizing the importance of an adequate financial structure, the Act (1) provides that bank holding companies can begin making equity investments in ETCs and (2) directs the Eximbank to establish a loan guarantee program for ETCs and other exporters. Progress in these areas has been slow, as described in the following sections.

Bank Holding Companies

In drafting the Act, Congress recognized that if ETCs were to be successful in promoting U.S. exports and in competing with foreign trading companies, they should be able to draw on the resources, expertise, and knowledge of the U.S. banking system. Accordingly, Title II of the Act states that:

> "The Congress hereby declares that it is the purpose of this title to provide for meaningful and effective participation by bank holding companies, bankers' banks, and Edge Act corporations 1/ [all referred to in this report as bank holding companies] in the financing and development of export trading companies in the United States."

Title II authorizes bank holding companies to make equity investments in ETCs but specifies that 60 days prior to such investments, the Federal Reserve Board (Board) is to be notified of the proposed investment. If the Board does not disapprove the investment within this time (which the Board may extend by 30 days if it needs additional information), the investment may be made. The Act specifies certain review criteria to be used by the Board in determining whether to disapprove the proposed investments.

Relatively Few Bank Investments

A Board representative advised that there are over 14,000 banking entities in the United States and that about 5,000 of these are bank holding companies. As of September 30, 1984, the Board had processed notifications involving 29 bank holding companies that proposed to make ETC investments totaling about $80 million. The 29 firms represent less than one percent of the bank holding companies but do include a number of the Nation's largest banking institutions. For

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1/ An Edge Act corporation is chartered and supervised by the Federal Reserve Board to engage in foreign or international banking or other foreign or international financial operations.

instance, 18 of the 29 firms rank in the largest 100 bank holding companies. No objections to any of the 29 proposed investments had been made by the Board.

We met with various banking and other business representatives and inquired about the reasons why there were relatively few ETC investments being made by the bank holding companies. Key reasons are cited below:

- The amount of profit and rate of return on ETC investments are too low.
- Some bankers believe the Act should provide tax advantages or other financial incentives to make ETC investments worthwhile.
- Various individuals are concerned that the Act and the Board's implementing regulations are unnecessarily restrictive in determining the kinds of ETCs which the banks may invest in. For example:
    - Banks may not invest in ETCs which export their services to foreign markets, although they can invest in ETCs which provide services designed to facilitate exports by other U.S. firms. Moreover, there are tight restrictions to be observed when a bank-affiliated ETC wants to take title to goods to be sold in overseas markets. Some individuals believe these restrictions make ETC investments less attractive to bankers.
    - Title II requires that investments be limited to ETCs which are exclusively engaged in activities related to international trade and which are organized and operated principally for purposes of exporting. The Board interprets this requirement to mean that the ETC must derive more than 50 percent of its revenues in each consecutive two-year period from export activities. In this regard, however, the Board does not count as export sales, revenues derived from countertrade where the U.S. seller is required to accept payment in the form of goods or other instruments of trade from third countries. Some business representatives consider the Board's decision to be an unusually restrictive interpretation of the Act and a disincentive to invest in ETCs.
- Certain ETCs do not want bank holding companies to invest in their firms for fear the banks will obtain operating control of the ETCs.

Indications are that many banks are adopting a wait-and-see approach regarding the desirability of ETC investments. After observing the results achieved by the first wave of banks to make ETC investments, we believe other banks can be expected to begin making judgments on this subject. Accordingly, it is too soon to gauge the Act's overall effect in helping to achieve the equity investment benefits envisioned by Congress.

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In response to our draft report, ITA commented about the universe of 5,000 bank holding companies and advised that:

> "...As a practical matter, the universe of qualified financial institutions with international experience, and the capability to form and operate an ETC is less than 400. Thus, about 10 percent of the real universe has already come forward and made equity investments in ETCs."

OIG Comment -- It is important to note that the Act does not limit ETC investments to only the bank holding companies with (1) international experience or (2) the capability to form and operate an ETC. Bank holding companies can simply invest in ETCs; there is no requirement to form and operate these firms. Even when it is decided to operate such firms, however, international experience can be acquired by hiring new personnel or by relying on the expertise available within newly acquired ETCs. For these reasons, we have simply reported the total number of bank holding companies, without refining or adjusting the universe of these firms.

Eximbank Loan Guarantees

Title II of the Act recognized the need to improve exporters' access to external financing and directed Eximbank to establish a loan guarantee program to:

> "...Provide guarantees for loans extended by financial institutions or other public or private creditors to export trading companies... or to other exporters, when such loans are secured by export accounts receivable or inventories of exportable goods, and when in the judgment of the Board of Directors -
>
> "(1) the private credit market is not providing adequate financing to enable otherwise credit-worthy export trading companies or exporters to consummate export transactions; and
>
> "(2) such guarantees would facilitate expansion of exports which would not otherwise occur.

> "The Board of Directors shall attempt to insure that a major share of any loan guarantees ultimately serves to promote exports from small, medium-size, and minority businesses or agricultural concerns..."

In accordance with the Act, Eximbank has established a working capital loan guarantee program for exporters to cover loans that would not otherwise be made available by commercial lenders. There are no established minimum or maximum guarantee amounts under this program. Eximbank will guarantee loans covering 90 percent of the principal amount of the loan, leaving the lender at risk for 10 percent. The borrower's collateral must be not less than 110 percent of the outstanding loan balance.

Level of Loan Guarantee Activity

Eximbank had made relatively few loan guarantees at the time of our review. Specifically, as of August 1, 1984, approvals had been given for 17 guarantees, totaling $20.2 million. Eximbank advised that each of the exporters receiving these guarantees was a small business or a business that was new to exporting.

We inquired about the reasons for the relatively small number of Eximbank loan guarantees. Feedback obtained from the ETCs and other business firms identified a number of reasons, as listed below.

- Some banks are unfamiliar with this new loan guarantee program and are unable to answer inquiries about it.
- Eximbank has no field office structure. This has made it more difficult for prospective applicants to obtain information about the program. We were informed that Eximbank sometimes invites interested parties to Washington, D.C. to discuss loan guarantee possibilities, but the time and expense of such trips discourages many prospective applicants.
- Some banks are concerned about the risks associated with export transactions.
- Some of the ETCs believe the paperwork involved in obtaining a loan guarantee is excessive and time consuming.
- According to several firms, Eximbank's 110 percent collateral requirement is excessive.

An Eximbank representative acknowledged that segments of the business community have been concerned about these issues and that Title II activity has been relatively limited. However, he pointed out that actions are underway to provide for more widespread use of the loan guarantee authority, as described below:

Recent Initiatives

New approaches were being implemented at the time of our audit to extend Eximbank's loan guarantee coverage. For instance, to help facilitate use of the loan guarantee program on a nationwide scale, Eximbank was interacting with the Small Business Administration (SBA) to provide for a cooperative approach by the two agencies in extending loan guarantees.

Under this cooperative venture, applicants need only submit application forms at their local SBA office for loan guarantees up to $1 million. (For amounts over $1 million, applications still must be submitted to Eximbank.) The new approach envisions that SBA will cover guarantees of $200,000 or less. If a guarantee exceeds that amount, SBA and Eximbank will share the entire amount of the guarantee, with each agency going up to a $500,000 limit. The agreement will help Eximbank to tie into the existing network of banks doing business with SBA.

In addition, Eximbank began a test-marketing campaign during mid-1984 covering a four-state area (Illinois, Michigan, Minnesota and Wisconsin). The objective is to try a number of initiatives in these four states and monitor progress in order to develop an improved national program for working capital loan guarantees. One of the initiatives to be tried out in these states will be the extension of delegated authority to commercial lenders, allowing them to approve Eximbank guarantees on working capital loans of up to $300,000 per qualified exporter.

Eximbank is obviously taking an active approach in trying to make its working capital loan guarantees available to a wider sector of the business community. We believe such initiatives are important if the loan financing objectives of the Act are to be achieved.

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We are offering no recommendations regarding the bank investment and loan guarantee functions being administered under Title II of the Act because Commerce has no direct management responsibility pertaining to these activities.

LITTLE DEMAND FOR THE ANTITRUST PROTECTION OFFERED BY CERTIFICATES OF REVIEW

Thousands of business representatives have attended seminars describing the advantages of the Act. However, at the close of FY 1984, only 63 organizations had sought the antitrust protection conferred by certificates of review authorized under Title III of the Act. Most of the ETCs that we visited had not applied for a certificate because they did not anticipate a need for such antitrust protection.

Regarding the processing of applications for certificates of review, OETCA has established a systematic approach for controlling and reviewing each incoming case. Working closely with the Office of General Counsel, OETCA has processed the applications in a thorough and timely manner.

Congressional Rationale in Authorizing Certificates of Review

The following comments prepared by the Office of General Counsel provide background about the business community's need for antitrust protection relating to export activities.

> "In its 1977 *Antitrust Guide for International Operations*, the Justice Department tried to reassure United States firms that wished to cooperate in export activities that their actions were beyond the jurisdiction of U.S. antitrust law so long as U.S. consumers and other independent exporters were not adversely affected by their actions. Nevertheless, some courts and commentators took positions inconsistent with the Justice Department's *Guide* on the basis of actions which seemingly would not invoke U.S. antitrust jurisdiction.
>
> * * * * * *
>
> "In these circumstances, it is not surprising that cautious antitrust counsel continued to veto joint export activities. The benefits of export cooperation simply did not seem worth the potentially ruinous consequences if antitrust errors were made.
>
> "Congress believed that the uncertain application of U.S. antitrust law to joint export activities and the risk of costly, time consuming litigation were significant deterrents to engaging in cooperative export trade. In a period when the U.S. merchandise trade deficit had become a

> foremost national concern, pressures mounted for legislative action to remove perceived impediments to exports of U.S. goods. To the extent our antitrust laws made it more difficult for U.S. companies to cooperate in developing overseas markets by sharing the costs and risks of export activities and other joint actions, Congress wanted those laws changed."

Accordingly, Title III of the Act authorizes Commerce, with Justice's concurrence, to issue certificates of review that provide limited antitrust immunity for certain export trade conduct. These certificates protect the holder and the members identified in the certificate from private treble damage actions and government criminal and civil suits under U.S. Federal and state antitrust laws for the export conduct specified in the certificates. Any person who has been injured by the certified conduct, however, may bring a suit for actual damages. Such suits are subject to specific limitations.

Level of Activity

Manufacturing and service firms have shown relatively little interest in obtaining Title III certificates of review. At the close of FY 1984, only 63 firms had applied for certificates. Of this total, 39 applications had been approved and the remainder were either being processed or had been returned to the applicant for additional supporting information. None of the applications had been denied.

The majority of applicants seeking antitrust protection have been small and medium-sized firms. Applicants include organizations which will export their own products and services, as well as those which will function as export trade intermediaries.

Reasons Why Firms Are Applying for Certificates of Review

Firms have varying reasons for applying for certificates of review. Some of them have no real antitrust problems, while others have genuine concerns about this subject.

We interviewed personnel at several of the firms which had received the certificates of review. Some of these firms were very small, and the managers acknowledged that the nature and scope of their current operations presented no antitrust concerns. However, these managers pointed out that the certificates provided a good insurance policy if antitrust issues should develop in the future. Nearly all the firms advised that an important reason for obtaining a certificate was to obtain increased stature and credibility in the business community. By publicizing their certified status, these organizations hoped to make a better impression with potential customers, thereby increasing their sales revenues.

OETCA advises, however, that many of the applicants have legitimate concerns about antitrust issues. In this regard, firms have sought antitrust protection for such export-related activities as:

- Allowing two or more companies to exchange confidential business information while preparing bids on overseas projects.
- Entering into exclusive sales and foreign distributorship agreements.
- Fixing prices for exports.
- Allocating export markets among specified U.S. firms.
- Cooperating and sharing information, as part of a joint export venture, through the vertical and horizontal integration of domestically competitive producers and processors.

A number of certificates have been approved for groups of domestic competitors that will be engaging in joint export activities to take advantage of the economies of scale and the sharing of risk that can result from cooperative efforts in the overseas markets. OETCA believes that, based on counseling experience and a review of recent application filings, there will be an increase in the percentage of applications involving joint ventures and joint export activities.

Reasons Why Firms Are Not Applying for Certificates

We interviewed various ETCs that had not applied for Title III certificates of review and inquired about the lack of interest. Basically, the firms advised that there was no reason to apply because they do not have any antitrust problems. In addition, some firms advised that the certificates have not yet been tested in court; consequently, these firms had doubts as to whether the certificates will stand the test of the judicial process.

Publicizing the Benefits of the Certificates

Under current procedures, OETCA uses the Federal Register to announce the receipt of each application for a Title III certificate of review. Likewise, when the certificate is approved, the Federal Register is used to announce the award and describe the conduct to be covered by the certificate. In addition, the Commerce publication, "Business America" has been used on a few occasions to describe how certain companies are planning to benefit from a Title III certificate. OETCA officials advised that ETC success stories will be publicized when information is available to show how firms have profited from ETC certificates.

Inasmuch as the first certificates were not issued until October 1983, there is limited experience regarding the effectiveness of the certificates in promoting and encouraging export trade. As previously mentioned, each recipient of a certificate is required to provide ITA with an annual report. Various kinds of information will be reported, including annual export sales data. The annual reports are only now starting to come due and relatively few have been received. Basically, the information received will be used to determine whether the certificate holders' activities and methods of operations are still in accordance with the overall terms of the Act and the specific provisions of the certificates.

ITA has no established way of determining the overall impact of the certificates in generating new export sales. An OETCA official advised that, in many cases, there is no realistic way to determine what portion of the certificate holders' export sales can be directly attributed to the certificates.

Processing Applications for Certificates of Review

Title III of the Act provides that, to qualify for a certificate of review, the applicant's export-related conduct must satisfy specified antitrust standards. Specifically, it must not:

- Substantially lessen competition or restrain trade in the United States nor substantially restrain the export trade of any competitor of the applicant;
- Unreasonably enhance, stabilize or depress prices in the United States;
- Be an unfair method of competition;
- Reasonably be expected to result in the sale or resale in the United States of the exported goods or services.

The Act specifies that a certificate can be issued to an applicant if the Secretary of Commerce, with the Attorney General's concurrence, determines that the above described standards are met. Also, the Act establishes a series of processing milestones to help ensure that a timely disposition is made of each incoming application. A final decision must be made on each application within 90 days after receipt at Commerce, unless the review process is interrupted because additional information is needed from the applicant.

Basically, we found that OETCA has established a systematic approach for processing and reviewing incoming applications. Under OETCA's management information system, incoming applications are tracked through each phase of the processing flow. This provides a ready reference source to determine whether legislatively mandated time limits are being adhered to.

All the applications that we tested had been thoroughly evaluated and had been processed within the required time frames. The review work includes close contact and interaction with the Office of General Counsel.

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We are making no recommendations relating to Commerce's role in administering the activities associated with Title III certificates of review.

ITA's response to our draft report provided the following comments:

> "In January 1985, two significant events took place which will have an effect on the future level of Title III activity. First, Commerce with Justice concurrence, issued the second edition of the Title III Guidelines. In their latest form, these Guidelines constitute a major statement of antitrust policy by the Departments of Commerce and Justice. They elaborate the departments' interpretation of the certification standards and describe how the departments will approach questions of technology licensing involving export trade, 'horizontal' and 'vertical' conduct by exporters and protections provided by the Certificate.
>
> "Later in the same month and, again, with the concurrence of Justice, the Department issued a certificate to a joint venture of four major U.S. producers of chlorine and caustic soda. The joint venture called Chlor/Alkali Producers International is comprised of B.F. Goodrich Company, Kaiser Aluminum and Chemical Corp., Occidental Chemical Corp., and Vulcan Materials Company.
>
> "Commerce has successfully implemented the Title III program. It has demonstrated the value of the Certificate process, and we have now seen major U.S. corporations taking advantage of this important new tool. As our export environment improves, it is logical to anticipate increased Title III activity."

ATTACHMENT

UNITED STATES DEPARTMENT OF COMMERCE
International Trade Administration
Washington, D.C. 20230

MAY 24 1985

MEMORANDUM FOR John R. Szpanka
Assistant Inspector General for Auditing

FROM: H. P. Goldfield

SUBJECT: Draft Report--Implementation of the Export Trading Company Program

We have reviewed the above referenced draft report and, with the exception of the following comments, are in general agreement with its content.

1. In commenting on the results of the legislation (page 9), the draft report appropriately notes that many of the persons interviewed pointed out that the development of the ETC network is still at a relatively early stage, and that it will take more time to develop a solid ETC structure. To provide a meaningful perspective, the report should also comment on the export environment that existed between the time the Act was passed and the time the draft report was prepared.

   In 1982, our trade deficit was $42.7 billion. By 1984, this deficit had climbed to $123.3 billion. This was a period marked by a strong dollar, a debt crisis in developing nations, and the illiquidity of several foreign currencies.

   In sum, this section of the draft report should point out that not only is it too early to measure results, but also that passage of the legislation coincided with the advent of a number of external events, which seriously impaired the ability of U.S. firms to compete effectively in export markets.

2. With regard to that portion of the draft report commenting on bank holding company equity investment in ETCs, we concur in the conclusion that "...it is too early to gauge the Act's overall effect in helping to achieve the equity investment benefits envisioned by Congress." (page 13) However, the introductory paragraphs to that portion of the draft report (page 11) convey an incorrect impression as to the universe of financial institutions capable of making an equity investment in a bank ETC.

Theoretically, it could be argued that, because there are about 5,000 bank holding companies in the United States, the appropriate universe of bank ETC candidates is 5,000 plus the existing Edge Act corporations and the bankers' banks. As a practical matter, the universe of qualified financial institutions with international experience, and the capability to form and operate an ETC is less than 400. Thus, about 10 percent of the real universe has already come forward and made equity investments in ETCs.

3. The final section of the draft report is focused heavily around the statement that there has been little demand for the antitrust protection offered by Certificates of Review. This opinion is open to debate. There are persons within the Department who were intimately involved in the legislative process who believe the level of Title III activity to date is approximately what was envisioned at the time of enactment. However, notwithstanding any disagreement as to what constitutes high or low demand, there are several factors which, for purposes of completeness and accuracy, should be contained in the report.

At the outset, the program was met with a degree of skepticism by members of the private antitrust bar. It was a new approach to providing antitrust protection for export activities and one which required applicants to reveal those proposed business activities sought to be protected. Many practitioners were uncertain whether the protection contained in the actual certificates receiving Department of Justice concurrence would be worth revealing their clients' business plans to Justice. Although the individualized counseling sessions conducted by OETCA included several Fortune 500 firms, none were included in the list of early applicants.

The situation has now changed. Commerce has now demonstrated that it can issue meaningful Certificates even where the applicants hold a relatively high market share and/or where the industry is relatively concentrated.

In January 1985, two significant events took place which will have an effect on the future level of Title III activity. First, Commerce with Justice concurrence, issued the second edition of the Title III Guidelines. In their latest form, these Guidelines constitute a major statement of antitrust policy by the Departments of Commerce and Justice. They elaborate the departments' interpretation of the certification standards and describe how the departments will approach questions of technology licensing involving export trade, "horizontal" and "vertical" conduct by exporters and protections provided by the Certificate.

Later in the same month and, again, with the concurrence of Justice, the Department issued a certificate to a joint venture of four major U.S. producers of chlorine and caustic soda. The joint venture called Chlor/Alkali Producers International is comprised of B. F. Goodrich Company, Kaiser Aluminum and Chemical Corp., Occidental Chemical Corp., and Vulcan Materials Company.

Commerce has successfully implemented the Title III program. It has demonstrated the value of the Certificate process, and we have now seen major U.S. corporations taking advantage of this important new tool. As our export environment improves, it is logical to anticipate increased Title III activity.

4. The statistics regarding the number of applications, certificates, bank ETCs, etc., are out of date and should be brought current at the time the final report is prepared.

Pursuant to memorandum dated May 9, 1985, prepared by Henry LeBlanc, Office of Domestic Operations, US&FCS, we have received the following US&FCS comments to the recommendations contained in the draft report:

RECOMMENDATIONS

1. Ensure that personnel in the district offices receive current information as to what they are expected to do in helping OETCA to promote and encourage the formation of ETCs. Also, provide for a clear understanding regarding the level of district office effort to be expended on ETC matters and the kind of performance reporting to be submitted relating to these activities.

RESPONSE

Domestic Operations welcomes the opportunity to develop a more close-knit working relationship with TD/OETCA to jointly promote the trading company concept. Specifically, district offices will continue to promote the ETC strategy as a means of getting smaller firms, unable or unwilling to export on their own, into international business. Trade specialists will also advise and assist organizations, including banks, who have a serious interest in becoming ETC operations. In order to carry out this endeavor, we would anticipate receiving additional guidance and new program materials as well as training for trade specialists from OETCA.

Under this recommendation, the following actions will be taken:

- A new Operations Bulletin will be issued (updating O.B. 83-75) to provide current information on what the role of district offices will be promoting and encouraging the formation of ETCs. Included will be a clarification of the respective roles to be played by OETCA and the field. In addition, guidelines and procedures will be included on how the US&FCS/Federal Bar Association agreement can be utilized to provide ETC legal counseling to business firms.
- A series of nine regional seminars on ETC will be planned during FY/86 (beginning in October 1985). The program and agenda will be prepared jointly by OETCA and US&FCS.
- The Management Planning Guidelines for Domestic Operations will be amended to specify that, among the mix of marketing strategies, an ETC component will be included when planning for the delivery of counseling services. This action will have the effect of measuring such efforts (under Critical Element II) against annual performance appraisals for Directors and other field personnel.
- The Business Counseling form (sample attached), used by trade specialists in reporting counseling sessions and actions, has been revised to include ETC data by type of account and export results reported. District office briefing reports will also include ETC activity when appropriate.

2. Provide district office personnel with appropriate training relating to ETC program matters.

RESPONSE

We fully endorse this recommendation. We will cooperatively work with OETCA in developing a training program that meets the specific needs of district office trade specialists.

3. Reassess the CFS listing to determine whether improvements can be made to increase the confidence level of business representatives in the usefulness of this listing.

RESPONSE

We are in general agreement on what the report says on the reception CFS has received from both business firms and the district offices. Some improvements are called for on both the criteria for registering firms on the CFS and the marketing of CFS. At this time, we will defer to OETCA to initiate such efforts. They have, in turn, agreed to provide improved guidelines which will be issued to the field in the Operations Bulletin mentioned above.

We appreciate the opportunity to comment on the draft report.

APPENDIX 4.—CORRESPONDENCE BETWEEN SECRETARY OF COMMERCE BALDRIGE AND FEDERAL RESERVE BOARD CHAIRMAN VOLCKER DURING 1983 AND 1984 CONCERNING FRB REGULATIONS

THE SECRETARY OF COMMERCE
Washington, D.C. 20230

SEP 21 1983

Honorable Paul A. Volcker
Chairman, Federal Reserve System
Washington, D.C. 20551

Dear Paul,

The Federal Reserve Board has recently published final regulations implementing Title II of the Export Trading Company (ETC) Act of 1982. Section 211.32(a) of the regulations contains the Board's definition of the term "export trading company." The definition adopted by the Board would preclude a bank-affiliated ETC from exporting its own services or from assuming a risk position when trading in goods for its own account.
This definition would limit a bank-affiliated ETC to providing trade facilitation services to unaffiliated companies. This is not the result intended by the language of the statute or the legislative history. It is contrary to the goals of this important legislation.

In the Conference Report for the ETC Act, Congress directed the Board to provide for meaningful participation by bank holding companies in the financing and development of ETCs so that they "will effectively and aggressively market American products and will not be disadvantaged or limited in competing with foreign-owned export trading companies or with ETCs owned by nonbank firms." I was actively involved in the passage of this legislation. In my opinion, the Congressional intent to promote the direct export of goods and services by bank-affiliated ETCs was very clear. Without the broadest possible participation of bank holding companies, early progress in ETC development will be diluted and the long-term objectives of the Act jeopardized.

I seek your cooperation in revising the regulatory definition of "export trading company" so that we may achieve the goals of the Export Trading Company Act.

Sincerely,

MAC

Secretary of Commerce

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

PAUL A. VOLCKER
CHAIRMAN

341291

October 24, 1983

The Honorable Malcolm Baldridge
Secretary of Commerce
Department of Commerce
Washington, D. C. 20230

Dear Mac:

In your letter of September 21 you expressed concern that Federal Reserve Board actions implementing the Bank Export Services Act (the "BESA") may limit the activities of a bank-affiliated export trading company in ways that are contrary to the goals of the legislation. I would like to correct what seems to me to be a misunderstanding of the Federal Reserve Board's regulations. I would also like to explain how we are implementing the BESA to carry out our common goal of encouraging United States exports through the growth of viable export trading companies in the United States.

Your letter states that the definition of export trading company adopted by the Board would preclude a bank-affiliated ETC from exporting its own services or from assuming a risk position when trading in goods for its own account. The second part of your concern -- limitations on taking title to goods -- can most easily be dealt with first. Both BESA and our regulations clearly authorize ETCs to undertake the key task of trading in goods, including explicitly taking title to goods themselves as part of the trading process.

The first part of your concern -- limitations on ETCs exporting their own services -- is more complicated to clarify. As I am sure you are aware, consistent with the express prohibitions of the BESA, a bank-affiliated ETC may not itself manufacture goods (with the minor exception of product modification) or engage in agricultural production. These ETCs may, however, freely take title to and trade in the products of others, and provide trade related services including marketing; advertising; financing; freight forwarding; transportation; product research and design; underwriting and selling insurance on the transportation of goods in international trade or other trade-related insurance on risks located or resident abroad.

In addition, the statute permits and our regulations encourage trading companies to take the form of joint ventures among banking organizations or among banking and nonbanking companies. Thus, if a commercial company, such as a producer of electronic equipment, and a bank holding company jointly establish an export trading company, that export trading company may trade in all of the goods manufactured by the commercial company co-investor.

Accordingly, a joint venture export trading company of an insurance company, or other "service" company, and a bank holding company are provided with full flexibility to sell the co-investor's insurance or other services abroad. Joint venture export trading companies also allow bank holding companies and American engineering, architectural and construction firms to meet their foreign competition by joining together in an export trading company to bid for and complete a specific project abroad, including a turnkey construction project, involving the export of a combination of goods and services of the co-investors.

Thus, based on this explanation of the broad scope of ETC activities, I think you will agree with me that bank holding company sponsored export trading companies have fully adequate operational flexibility to carry out their functions as envisaged by the BESA. The only difference we seem to have concerns the ability of these ETCs to engage directly in a relatively narrow range of activities outside of manufacturing and agricultural production, which are expressly prohibited, but which activities are not included within the broad range of export trade services that are expressly authorized by the Act and our regulations. Although the scope of excluded services is narrow, there are two important reasons why these other activities should not be authorized for bank-affiliated ETCs.

First, such an authorization could defeat Congress' intention in passing the BESA of departing from the basic rule of separating banking from commerce to the extent necessary to place banks in the role of facilitators of the exports of American producers. Although Congress sought to encourage banking organization participation in export trading companies, we see no evidence of an intention to give them the authority to make equity investments in an unlimited range of production and service companies such as in mining companies, oil and gas developers, architects' offices, engineering companies and general insurance underwriters to provide these services for export. Indeed, a conscious decision was made that bank-affiliated ETCs in the United States would not have as broad a scope of authority as Japanese trading companies, for example, or nonbank affiliated ETCs in the United States.

Second, Congress established these new types of U.S. trading companies to take advantage of a bank's network of overseas offices, international experience, domestic customer base, and trade financing capabilities. The objective was to facilitate the finding and expansion of new export markets for U.S. firms, particularly the medium-sized and smaller companies that could not provide these services from their own resources. There is no indication that Congress intended that the ETC authority would be used to authorize direct bank participation in production of goods and services for export as distinguished from the use of their special capabilities to promote the exports of American producers. Indeed, providing services to foreign customers may not involve the performance of any significant activities in the United States or remittance of profits here and so have little real effect on U. S. exports.

I know of no problems that have arisen regarding banking participation in ETCs because of an inadequate scope of authority for those trading companies. I am particularly pleased that the Board was able to implement the BESA so quickly, despite the unique provisions of the law and formative stage of this U. S. industry. Twelve bank holding companies already are investing in export trading companies under the BESA, and several more proposed investments are under review under the expedited procedures prescribed by the Act. The investments are by banking organizations of varying sizes, from a number of geographic regions, and represent a variety of approaches to utilizing the authority under the Act.

I hope that this letter is helpful to you in explaining our approach to a positive and effective implementation of the BESA. Please be assured of our full cooperation in working out any other problems or misconceptions that may develop.

Sincerely,

Paul

P.S. If you have lingering doubts, please give me a call. Pau

THE SECRETARY OF COMMERCE
Washington, D.C. 20230

SEP 13 1984

Honorable Paul A. Volcker
Chairman, Federal Reserve System
Washington, D.C. 20551

Dear Paul,

I would like to express to you my continued concern with the Federal Reserve Board's regulations for the Bank Export Services Act ("ETC Act"). These regulations unduly restrict the opportunities available to bank-affiliated export trading companies. In addition, the Board appears to be narrowing the powers of such ETCs in areas not specifically required by the regulations. For example, I am disappointed that under the Board's ETC approvals, bank-affiliated ETCs have not been able to freely take title to goods. They have been limited to taking title against firm orders, except for an inventory up to $2 million. Unlike non-bank-affiliated and foreign counterparts, U.S. bank ETCs may not assume risk positions commonly accepted in international trade.

The Board has given several reasons for its narrow interpretation of the statutory definition of "export trading company." First, it has stated that Congress intended in the ETC Act to relax the rule separating banking and commerce only to the extent necessary to place banks in the role of facilitators of U.S. exports. Second, the Board has asserted that there is no indication that Congress intended bank-affiliated ETCs to export their own services. You have also stated that service exports may not be of benefit to the U.S. economy.

I agree that in the ETC Act Congress carefully considered the extent to which the rule separating banking and commerce would be altered. The primary reason for this rule is the protection of bank depositors, and the ETC Act contains several well-designed safeguards to meet this concern, including limitations on eligible bank-affiliated investors, amounts of equity investments, and loans to ETC's. In addition, the Board may disapprove any proposed investment if necessary to prevent unsafe or unsound banking practices. I am aware that examining each proposed investment in an ETC for its possible effect on bank safety could prove administratively burdensome. However, the ETC Act contemplates just such an analysis. The Department of Commerce is willing to assist your staff in drawing up guidelines to ease any potential burden. It is not necessary to manipulate the definition of "export trading company" to deal with concerns for bank safety.

I cannot agree with the second reason given for restricting the authority of bank-affiliated ETCs: providing services to foreign customers has little real effect on U.S. exports. The export of U.S.-produced services is of great benefit to the U.S. economy and of great importance in the implementation of the ETC Act. Congress explicitly found in Section 102(a) of the ETC Act that service-related industries" are vital to the well-being of the United States economy ... and offer the greatest potential for significantly increased trade involving finished products." We can supply you with much material developed by the Department of Commerce supporting this finding. The Department of Commerce shares the view of Congress expressed in the statute and I request your cooperation in carrying out the statutory intent.

I also disagree that there is no indication that Congress intended a bank-affiliated ETC to have the authority to export its own services. Legal research by our Office of General Counsel has found much evidence that Congress clearly understood that bank-affiliated ETCs would export their own services. And those who supported the passage of the legislation thought that this was one of the powers they would receive. See the enclosed testimony of Arthur P. Sultan, Chief Administrative Officer of Citicorp International Trading Company, recently given before Congressman Bonker's Subcommittee on International Economic Policy and Trade.

Once again I urge the Board to work with the Department of Commerce to develop a definition of "export trading company" and address other issues raised by the ETC Act in a manner which will "provide for the establishment of export trading companies with powers sufficiently broad to enable them to compete with similar foreign-owned institutions in the United States and abroad" (Section 202 of the ETC Act). You will have our full cooperation in attaining this goal. At your earliest convenience, let's discuss these issues further.

Sincerely,

Mac

Secretary of Commerce

Enclosure

RECEIVED
OFFICE OF THE
GENERAL COUNSEL
OCT 10 3 07 PM '84

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D.C. 20551

PAUL A. VOLCKER
CHAIRMAN

October 9, 1984

The Honorable Malcolm Baldridge
Secretary of Commerce
Department of Commerce
Washington, D.C. 20230

Dear Mac:

In your letter of September 13, 1984, you expressed continuing concern regarding some of the Board's policies and rules administering the Bank Export Services Act (BESA). We have also been focusing on the BESA in the context of reviewing the Board's report to Congress on experience in administering the Act over the past two years. I am enclosing a copy of this report which I think you will find useful for its analysis of the scope of bank export trading company activities and as an explanation of the policies adopted by the Board in applying the Act. I was concerned, however, because your most recent letter contains some misunderstandings of several of the positions taken by the Board and I would like to take your time for a moment to address these issues.

At the outset, I would like to express the Board's support for what I believe is our shared goal of improving the export performance of our economy. As I know you are aware, there are many steps that could be taken to accomplish this objective, and the necessary measures are, of course, an important factor in the Board's deliberations on economic policy issues. This recognition of the importance of U.S. export performance carries into our administration of the BESA as one vehicle for promoting this objective. We have, and will continue to apply the provisions of the BESA so as to assure that banking organizations have the opportunity to make a significant contribution to export growth.

I sense, however, from your letter a general frustration that in the two years since the Export Trading Company Act was passed there has not been a greater industry response to the legislation. When the law was enacted, there may have been some overly optimistic expectations as to the pace at which we would see development of this new enterprise in the United States on a wide scale. Since most U.S. businesses in general, and banking organizations in particular, were not familiar with the operations of trading companies, their involvement with them could not be expected to develop in a substantial way in the short-term.

Moreover, in the two years since the law's enactment, world economic conditions have not been particularly favorable for the development of the export trading company business in the United States. Indeed, some export trading companies that have been formed without bank affiliation (and thus are not subject to the BESA rules) have indicated that the profitability of the ventures must look toward longer time horizons. For example, the Chairman of Sears, Roebuck and Co., the parent of Sears World Trade, Inc., was reported recently as stating that Sears may need "10 to 15 years to be a meaningful player [as a trading company]" but that Sears will have the staying power to succeed. Similarly, from the experience with bank export trading companies, I am impressed with the need for our businessmen to develop over time the foundation upon which substantial export gains can be achieved.

Nevertheless, I feel there is positive news to report that the necessary start is being made. Despite the economic and business difficulties in developing export trading companies, the bank holding company reaction thus far has been quite positive: 29 banking organizations of varying size and geographic location have become affiliated with export trading companies, with investments aggregating approximately $80 million. Based on projections submitted with their notifications, the bank holding companies estimate that by year-end 1985 the total assets of these export trading companies may approach $600 million.

Turning to the specific points raised in your letter concerning the regulations adopted by the Board, I would like to emphasize that, contrary to your impression, export trading companies ("ETCs") in which banking organizations may invest under the BESA are not prohibited from taking title to goods except against firm orders. Rather, the regulations provide generally for Board review of proposed investments in ETCs that plan to take title to goods other than against firm orders. The rules involve the Board's recognition of the fact that taking positions in goods involves sufficient risk that the Board should have the opportunity to review carefully proposals that involve this activity, and to disapprove those proposals that could involve unsafe and unsound practices (for example, where the ETC has an inadequate system of management controls), or where the ETC has insufficient safeguards to protect against violation of the statutory prohibition against speculation in commodities (12 U.S.C. § 1843(c)(14)(D)). A more complete technical explanation of the regulation is enclosed.

In your letter you also stated your disagreement with the definition of an "export trading company" adopted in the Board's implementing regulations. You have suggested a broader definition under which a bank-affiliated export trading company would be able to export services of any kind. On this point, I am concerned that your letter reflects an apparent misperception that, in adopting a rule allowing for a more limited range of service exports, the Board did not recognize the value to the U.S. economy of exports of U.S. services. The issue the Board addressed in implementing the BESA was not whether the export of services is important to the U.S. economy -- the Board, of course, recognizes its importance -- but, rather, whether export trading companies affiliated with U.S. banking organizations were authorized by the BESA to act as principals in the export of any kind of services.

We have reviewed your staff's legal analysis and their arguments that the scope of activities permissible for ETCs under Title II (the BESA), which the Federal Reserve administers, is co-extensive with those permissible under Title I of the Export Trading Company Act, which the Commerce Department administers. Our staff analysis differs on this point. Aside from the technicalities of the legal analysis, I feel that it is clear, from my own knowledge of the legislative debate on the BESA and from subsequent Congressional consideration of bank holding company legislation, that Congress would not regard banking organization investments in construction companies, general insurance underwriters, or mining companies, for example, as within the scope of activities authorized by the BESA. This record amply demonstrates that Congress did not alter so fundamentally the scope of services in which bank holding companies might engage outside of the United States as to permit the sale of any service so long as it is provided to a foreign client through a subsidiary nominally called on "export trading company."

This does not mean that bank-affiliated export trading companies cannot perform a very wide range of services to facilitate trade -- they can, and these services can be provided to U.S. residents as well as foreigners. An extensive list of permissible trade services is contained in the BESA, and it includes consulting, marketing, financing, transportation, certain forms of trade insurance, warehousing, and other activities. Moreover, this list is not exclusive, and other trade intermediation activities may be authorized by the Board.

I hope this letter clarifies any misunderstandings you may have had regarding the Board's policies and regulations. Please give me a call when you have an opportunity so that we can discuss these questions further.

Sincerely,

Paul

Enclosures

ENCLOSURE

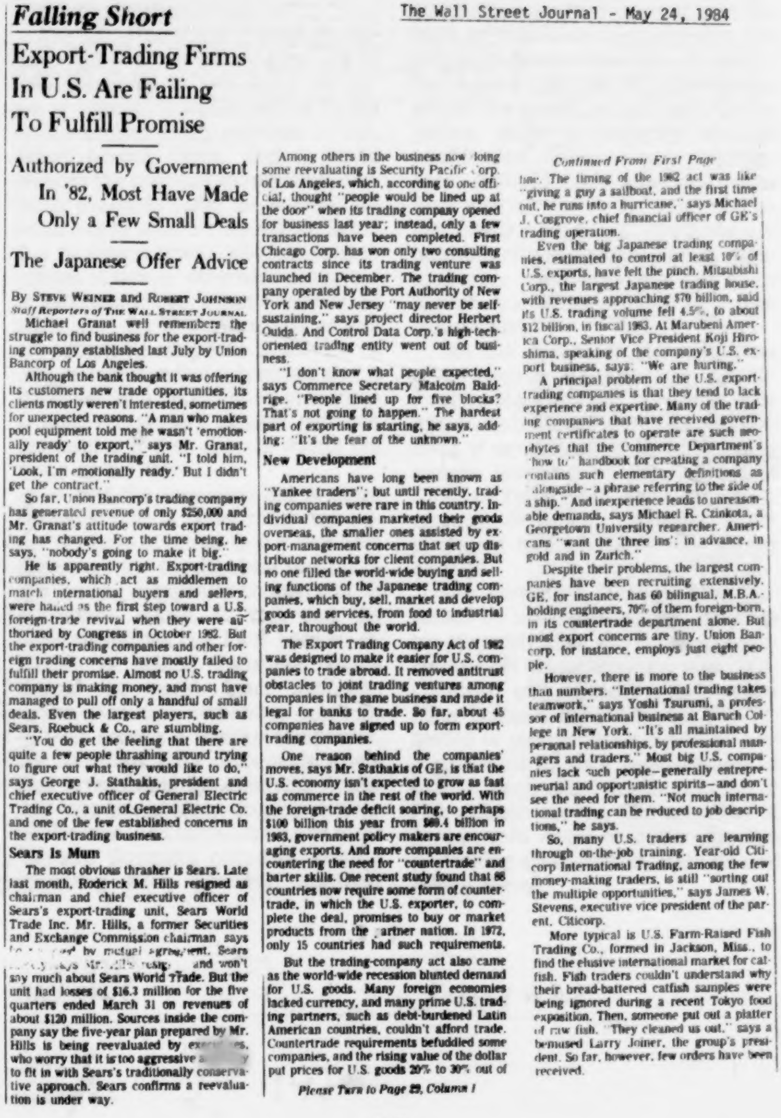
References in Federal Reserve regulations to "taking title to goods"

One section of the regulations prescribes procedures for filing and processing notices of proposed investments in ETCs and states that an investor shall give the Board prior notice of changes in the activities of an ETC that is a subsidiary of the investor if the ETC expands its activities beyond those described in the initial notice of the investment to include: (1) taking title to goods other than against firm orders; (3) product research and design; (3) product modification; or (4) activities not listed in section 4(c)(14)(F)(ii) of the Bank Holding Company Act. 12 C.F.R. § 211.34a(2)(i). The purpose of this provision of the regulation is not to prohibit an ETC in which a banking organization invests from engaging in any of the foregoing activities. Rather, it merely establishes a procedure for effective Board review of proposed investments where the character and scope of activities in which the ETC intends to engage changes substantially from those described in the initial notice of investment.

Another procedural provision of the Board's regulations refers to taking title to goods. One of the criteria establishing whether a notice to invest in an ETC may be delegated to the appropriate Federal Reserve Bank, rather than reviewed by the Board, is that "the proposed export trading company will take title to goods only against firm orders, except that the company may maintain an inventory of goods worth up to $2 million." 12 C.F.R. § 265.2(f)(58)(iii). Again, this provision does not prohibit taking title to goods except against firm orders, rather it merely requires the proposal to be reviewed by the Board.

APPENDIX 5.—PRESS MATERIALS

A. "FALLING SHORT: EXPORT-TRADING FIRMS IN U.S. ARE FAILING TO FULFILL PROMISE," STEVE WEINER AND ROBERT JOHNSON, THE WALL STREET JOURNAL, MAY 24, 1984



The Wall Street Journal - May 24, 1984

Falling Short

Export-Trading Firms In U.S. Are Failing To Fulfill Promise

Authorized by Government In '82, Most Have Made Only a Few Small Deals

The Japanese Offer Advice

By STEVE WEINER and ROBERT JOHNSON
Staff Reporters of THE WALL STREET JOURNAL

Michael Granat well remembers the struggle to find business for the export-trading company established last July by Union Bancorp of Los Angeles.

Although the bank thought it was offering its customers new trade opportunities, its clients mostly weren't interested, sometimes for unexpected reasons. "A man who makes pool equipment told me he wasn't 'emotionally ready' to export," says Mr. Granat, president of the trading unit. "I told him, 'Look, I'm emotionally ready.' But I didn't get the contract."

So far, Union Bancorp's trading company has generated revenue of only $250,000 and Mr. Granat's attitude towards export trading has changed. For the time being, he says, "nobody's going to make it big."

He is apparently right. Export-trading companies, which act as middlemen to match international buyers and sellers, were hailed as the first step toward a U.S. foreign-trade revival when they were authorized by Congress in October 1982. But the export-trading companies and other foreign trading concerns have mostly failed to fulfill their promise. Almost no U.S. trading company is making money, and most have managed to pull off only a handful of small deals. Even the largest players, such as Sears, Roebuck & Co., are stumbling.

"You do get the feeling that there are quite a few people thrashing around trying to figure out what they would like to do," says George J. Stathakis, president and chief executive officer of General Electric Trading Co., a unit of General Electric Co. and one of the few established concerns in the export-trading business.

Sears Is Mum

The most obvious thrasher is Sears. Late last month, Roderick M. Hills resigned as chairman and chief executive officer of Sears's export-trading unit, Sears World Trade Inc. Mr. Hills, a former Securities and Exchange Commission chairman says [illegible] by mutual agreement. Sears [illegible] says Mr. Hills resigned and won't say much about Sears World Trade. But the unit had losses of $16.3 million for the five quarters ended March 31 on revenues of about $120 million. Sources inside the company say the five-year plan prepared by Mr. Hills is being reevaluated by executives, who worry that it is too aggressive [illegible] to fit in with Sears's traditionally conservative approach. Sears confirms a reevaluation is under way.

Among others in the business now doing some reevaluating is Security Pacific Corp. of Los Angeles, which, according to one official, thought "people would be lined up at the door" when its trading company opened for business last year; instead, only a few transactions have been completed. First Chicago Corp. has won only two consulting contracts since its trading venture was launched in December. The trading company operated by the Port Authority of New York and New Jersey "may never be self-sustaining," says project director Herbert Ouida. And Control Data Corp.'s high-tech-oriented trading entity went out of business.

"I don't know what people expected," says Commerce Secretary Malcolm Baldrige. "People lined up for five blocks? That's not going to happen." The hardest part of exporting is starting, he says, adding: "It's the fear of the unknown."

New Development

Americans have long been known as "Yankee traders"; but until recently, trading companies were rare in this country. Individual companies marketed their goods overseas, the smaller ones assisted by export-management concerns that set up distributor networks for client companies. But no one filled the world-wide buying and selling functions of the Japanese trading companies, which buy, sell, market and develop goods and services, from food to industrial gear, throughout the world.

The Export Trading Company Act of 1982 was designed to make it easier for U.S. companies to trade abroad. It removed antitrust obstacles to joint trading ventures among companies in the same business and made it legal for banks to trade. So far, about 45 companies have signed up to form export-trading companies.

One reason behind the companies' moves, says Mr. Stathakis of GE, is that the U.S. economy isn't expected to grow as fast as commerce in the rest of the world. With the foreign-trade deficit soaring, to perhaps $100 billion this year from $69.4 billion in 1983, government policy makers are encouraging exports. And more companies are encountering the need for "countertrade" and barter skills. One recent study found that 88 countries now require some form of countertrade, in which the U.S. exporter, to complete the deal, promises to buy or market products from the partner nation. In 1972, only 15 countries had such requirements.

But the trading-company act also came as the world-wide recession blunted demand for U.S. goods. Many foreign economies lacked currency, and many prime U.S. trading partners, such as debt-burdened Latin American countries, couldn't afford trade. Countertrade requirements befuddled some companies, and the rising value of the dollar put prices for U.S. goods 20% to 30% out of

Please Turn to Page 29, Column 1

Continued From First Page

line. The timing of the 1982 act was like "giving a guy a sailboat, and the first time out, he runs into a hurricane," says Michael J. Cosgrove, chief financial officer of GE's trading operation.

Even the big Japanese trading companies, estimated to control at least 10% of U.S. exports, have felt the pinch. Mitsubishi Corp., the largest Japanese trading house, with revenues approaching $70 billion, said its U.S. trading volume fell 4.5%, to about $12 billion, in fiscal 1983. At Marubeni America Corp., Senior Vice President Koji Hiroshima, speaking of the company's U.S. export business, says: "We are hurting."

A principal problem of the U.S. export-trading companies is that they tend to lack experience and expertise. Many of the trading companies that have received government certificates to operate are such neophytes that the Commerce Department's "how to" handbook for creating a company contains such elementary definitions as "alongside – a phrase referring to the side of a ship." And inexperience leads to unreasonable demands, says Michael R. Czinkota, a Georgetown University researcher. Americans "want the 'three ins': in advance, in gold and in Zurich."

Despite their problems, the largest companies have been recruiting extensively. GE, for instance, has 60 bilingual, M.B.A.-holding engineers, 70% of them foreign-born, in its countertrade department alone. But most export concerns are tiny. Union Bancorp, for instance, employs just eight people.

However, there is more to the business than numbers. "International trading takes teamwork," says Yoshi Tsurumi, a professor of international business at Baruch College in New York. "It's all maintained by personal relationships, by professional managers and traders." Most big U.S. companies lack such people—generally entrepreneurial and opportunistic spirits—and don't see the need for them. "Not much international trading can be reduced to job descriptions," he says.

So, many U.S. traders are learning through on-the-job training. Year-old Citicorp International Trading, among the few money-making traders, is still "sorting out the multiple opportunities," says James W. Stevens, executive vice president of the parent, Citicorp.

More typical is U.S. Farm-Raised Fish Trading Co., formed in Jackson, Miss., to find the elusive international market for catfish. Fish traders couldn't understand why their bread-battered catfish samples were being ignored during a recent Tokyo food exposition. Then, someone put out a platter of raw fish. "They cleaned us out," says a bemused Larry Joiner, the group's president. So far, however, few orders have been received.

Duane L. Repp, president of D.M.T. World Trade Inc., Waukesha, Wis., sells electric motors and pumps but has found it isn't always easy to get what the customer wants. For example, a Saudi Arabian businessman has asked him to find a machine to make lollipops; but so far, Mr. Repp has failed in that task.

Most corporate-trading arms tend to concentrate on countertrade for the company's own products. C-E Trading Inc., for instance, trades in such diverse items as machine tools, minerals, palm oil, fertilizer and shoes to further the business of its parent, Combustion Engineering Corp. But Honeywell Inc.'s trading unit, Honeywell High-Tech Trading Inc., also sells goods and services from other concerns in related electronic lines, carving out a comfortable niche by using an existing distribution system. So far, Honeywell has signed 21 sales agreements with other companies.

Such deals with non-exporting companies are the bulk of business being sought by bank-exporting companies. An estimated 20,000 companies could export products but don't. Even so, some bankers aren't certain how to apply their international financial experience to actual trading. "We're going up against formidable opponents everywhere," says Peter M. Nelson, president of BankAmerica Corp.'s trading company. "I don't think we're going to be very big in a couple of years."

GE Trading, the largest U.S. trading company, won't be profitable until 1985, President Stathakis says. Begun in 1982, its volume last year was $500 million, plus countertrade in support of other GE exports valued at about $800 million. Such countertrade and the company's existing export base of about $4 billion a year are the trading company's foundation.

About 90% of GE Trading's exports are the company's own products. But the company plans to grow into new areas. Already, its countertrade needs have pushed it into metals markets, and Mr. Cosgrove, the financial officer, says GE Trading may make acquisitions this year, possibly in the financial-services and general-commodity areas.

It is a company built on an entrepreneurial and opportunistic base with a goal of becoming a general trading enterprise. "The only limitations on trading are your own imagination and the ability to put together a deal," Mr. Cosgrove says.

GE Trading's biggest coup was a complex barter deal with Romania that saved a $150 million sale of two turbine generators. When the deal appeared to fail because of a Romanian monetary crisis in 1982, GE Trading agreed to take half of its payment in such goods as nails and television sets. "It's the first nuclear-power plant in the world to be paid for in nails," quips P.A. "Tak" Argentinis, GE's countertrade chief.

As a general trader with an immense consumer base, Sears World Trade is the better known of trading companies, and its goals have been vast. "The scope of our ambition is as large as any of the Japanese trading companies," Mr. Hills said in an interview earlier this year.

Sears World Trade wants to be able to provide any product which any customer might want anywhere. It buys and sells lumber products world-wide, offers management consulting services, supplies goods for other retail chains. It finds ways for developing countries and businesses to improve their products, making them more suitable for world trade. It finds buyers and provides financial, insurance and shipping services. "We add value to articles of trade," Mr. Hills said in the interview.

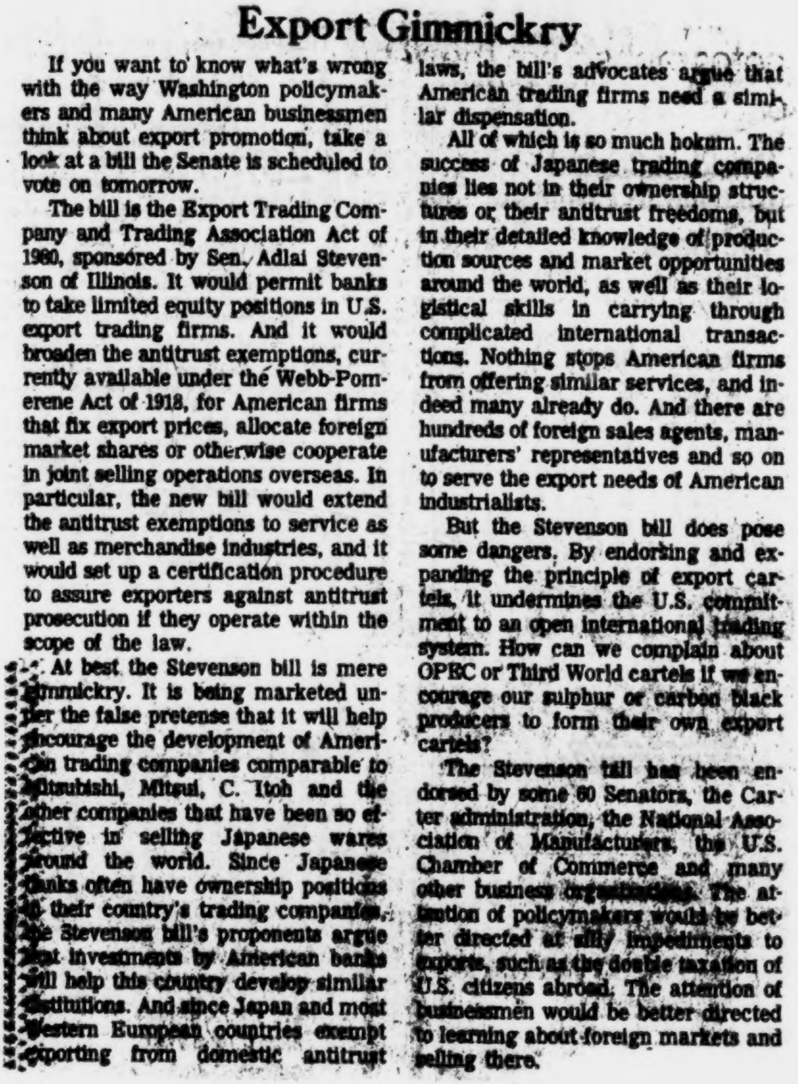
Sears originally saw its trading company as an importer and exporter of consumer goods that would build on the company's world-wide base of suppliers. Mr. Hills, named chairman in October 1982, instead molded a general trading company with a broader focus on consumer, high-tech, health and agricultural goods and services.

Despite the losses, Sears World Trade was progressing according to plan, insiders say. Joint ventures had been formed in Germany, Italy, Hong Kong, the Philippines and England. "We established a distinguished global presence," Mr. Hills says. But the trading company was moving too quickly and with too little assurance of success for some senior Sears officers.

"The issue is what the scope of the activity should be," one insider says. "I'm not sure (senior officers) appreciate that one has to get out in the water, negotiate and make deals. You've got to have a lot of faith."

Japanese traders say it will be hard work and slow growth that make the most successful U.S. trading houses. "Even for us, it took more than 100 years," says Shinichiro Wada, a division manager for Mitsubishi International Corp., New York. The U.S. export companies "are still groping, but it's premature to say whether they're going to be successful," says Mr. Hiroshima of Marubeni. "I haven't heard any success stories yet, but give it time."

B. "EXPORT GIMMICKRY," EDITORIAL, THE WALL STREET JOURNAL, SEPTEMBER 2, 1980



Export Gimmickry

If you want to know what's wrong with the way Washington policymakers and many American businessmen think about export promotion, take a look at a bill the Senate is scheduled to vote on tomorrow.

The bill is the Export Trading Company and Trading Association Act of 1980, sponsored by Sen. Adlai Stevenson of Illinois. It would permit banks to take limited equity positions in U.S. export trading firms. And it would broaden the antitrust exemptions, currently available under the Webb-Pomerene Act of 1918, for American firms that fix export prices, allocate foreign market shares or otherwise cooperate in joint selling operations overseas. In particular, the new bill would extend the antitrust exemptions to service as well as merchandise industries, and it would set up a certification procedure to assure exporters against antitrust prosecution if they operate within the scope of the law.

At best the Stevenson bill is mere gimmickry. It is being marketed under the false pretense that it will help encourage the development of American trading companies comparable to Mitsubishi, Mitsui, C. Itoh and the other companies that have been so effective in selling Japanese wares around the world. Since Japanese banks often have ownership positions in their country's trading companies, the Stevenson bill's proponents argue that investments by American banks will help this country develop similar institutions. And since Japan and most Western European countries exempt exporting from domestic antitrust laws, the bill's advocates argue that American trading firms need a similar dispensation.

All of which is so much hokum. The success of Japanese trading companies lies not in their ownership structures or their antitrust freedoms, but in their detailed knowledge of production sources and market opportunities around the world, as well as their logistical skills in carrying through complicated international transactions. Nothing stops American firms from offering similar services, and indeed many already do. And there are hundreds of foreign sales agents, manufacturers' representatives and so on to serve the export needs of American industrialists.

But the Stevenson bill does pose some dangers. By endorsing and expanding the principle of export cartels, it undermines the U.S. commitment to an open international trading system. How can we complain about OPEC or Third World cartels if we encourage our sulphur or carbon black producers to form their own export cartels?

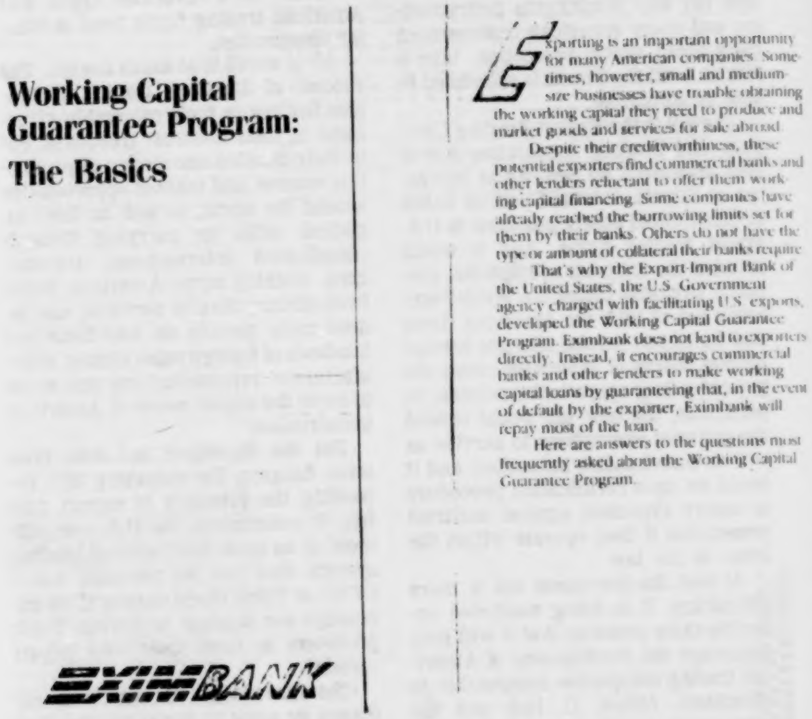
The Stevenson bill has been endorsed by some 60 Senators, the Carter administration, the National Association of Manufacturers, the U.S. Chamber of Commerce and many other business organizations. The attention of policymakers would be better directed at silly impediments to exports, such as the double taxation of U.S. citizens abroad. The attention of businessmen would be better directed to learning about foreign markets and selling there.

Wall St. Journal

Sept. 2, 1980

APPENDIX 6.—MATERIAL CONCERNING THE EXPORT-IMPORT BANK'S WORKING CAPITAL GUARANTEE PROGRAM

A. BASIC DESCRIPTION OF THE PROGRAM



Working Capital Guarantee Program: The Basics

EXIMBANK

Exporting is an important opportunity for many American companies. Sometimes, however, small and medium-size businesses have trouble obtaining the working capital they need to produce and market goods and services for sale abroad.

Despite their creditworthiness, these potential exporters find commercial banks and other lenders reluctant to offer them working capital financing. Some companies have already reached the borrowing limits set for them by their banks. Others do not have the type or amount of collateral their banks require.

That's why the Export-Import Bank of the United States, the U.S. Government agency charged with facilitating U.S. exports, developed the Working Capital Guarantee Program. Eximbank does not lend to exporters directly. Instead, it encourages commercial banks and other lenders to make working capital loans by guaranteeing that, in the event of default by the exporter, Eximbank will repay most of the loan.

Here are answers to the questions most frequently asked about the Working Capital Guarantee Program.

Answers to Your Questions

1. What businesses are eligible for the Working Capital Guarantee Program?

The Working Capital Guarantee was specifically developed to promote exports by small, medium-size, minority and agricultural concerns. It may, however, be used to cover working capital loans made to any U.S. business as long as the lender certifies that the guarantee is essential for the loan to go forward and Eximbank determines that the exporter is creditworthy.

2. Which lenders can apply for Eximbank's Guarantee?

Any bank or provider of private credit is eligible for the program as long as Eximbank determines that the lender has the ability and resources to service the loans.

3. Does the guarantee apply to revolving lines of credit?

Yes, the program guarantees loans for revolving credit lines as well as loans for specific transactions.

4. What are acceptable uses of the loan proceeds?

Loan funds may be used to purchase materials, products, services and labor for production of goods or services for current or future export sales. Loan funds may also be used for foreign business development such as marketing activities, trade fair participation or other promotional activities. The guarantee is meant to foster additional export sales and will not cover loans used to pay existing debts.

5. What are the terms and conditions of the loan?

The term of the loan is generally up to twelve months and may be extended. Because Eximbank's intent is to facilitate exports that would not have occurred otherwise, the lender must certify that the loan would not be made without Eximbank's guarantee. Eximbank does not impose any interest rate ceilings or limits on fees the lender may charge. It expects, however, that pricing will reflect the fact that most risks are covered by an agency of the U.S. government.

6. How much of the loan is covered by the Guarantee?

Eximbank guarantees 90 percent of the principal amount of the loan as well as interest, up to the date of claim payment. Interest covered is at the stated rate on the loan or one percent above the U.S. Treasury borrowing rate for comparable maturities, whichever is lower. The lender retains the risk on the remaining 10 percent of the loan and any interest above the guaranteed rate.

7. What are the collateral requirements?

Eximbank requires that the loan balance not exceed 90% of the collateral value. Acceptable collateral includes goods and services purchased with the proceeds of the guaranteed loan as well as accounts receivable resulting from transactions generated by the loan. Other types of collateral will also be considered.

8. What fees does Eximbank charge for the guarantee?

The fee depends on the length and amount of the loan. If the guarantee period is less than six months, the fee is 1.0 percent of the loan amount. For periods of six months to one year, the fee is 1.5 percent of the loan amount. Fees are payable in a lump sum when Eximbank issues its guarantee.

9. Who is protected by the Working Capital Guarantee?

The Working Capital Guarantee protects the lender against default by the exporter. It does not protect the exporter against default by foreign buyers. For this reason, exporters and their lenders should determine whether they need credit risk protection on foreign receivables.

10. What is the application procedure?

Application is made by the lender and must include detailed financial data about the exporter. Lenders should call Eximbank for application forms and instructions at (202) 566-8819. Exporters who want assistance finding lenders interested in the program should call their local U.S. Department of Commerce Office or Eximbank's Business Advisory Hotline (800-424-5201).

January 1985

B. EXPORTERS' AND EXPORT TRADING COMPANIES' LETTERS TO THE SUBCOMMITTEE

TWP

TRANS WORLD PRODUCTS CO., INC.
Export Trading
1776 K STREET, N.W., SUITE 507
WASHINGTON, D.C. 20006
Telephone (202) 232-9024, (202) 887-5360, (202) 887-5361
Telex NR 904102 TWP CO., INC WSH

March 3, 1986

RECEIVED
MAR 4 1986
COMMERCE, CONSUMER AND
MONETARY AFFAIRS SUBCOMMITTEE

Hon. Doug Barnard, Jr.
Chairman
Subcommittee on Commerce, Consumer,
and Monetary Affairs of the
Committee on Government Operations
Room B-377, RHOB
Washington, D.C. 20515

Dear Chairman Barnard:

I am very pleased to submit the following statement which details the experience of our company, Trans World Products Co., Inc. ("TWP") in terms of the utility and effectiveness of the Export Trading Act of 1982 as well as a review of our experience with the federal agencies with which we have dealt in matters related to the implementation of the provisions of the Act.

Briefly, TWP was incorporated in January 1982 with the specific objective of specializing in international trade and other related activities. Between 1982 and 1984 TWP had firm transactions in the form of irrevocable letters of credit for over $8 million (see enclosed copies of LCs). All orders except one were for the export of U.S. goods. By our estimate, these orders could have created over 150 jobs in the U.S., particularly in the farm belt. Perhaps our orders could have helped stave a farmer or two from bankruptcy, as well as made a small dent in the enormous U.S. trade deficit. TWP's area of prime concentration is in the export of agricultural commodities -- wheat, wheat flour, rice, sugar, vegetable oil, etc. The unfilled orders would have been repeat business; thus our estimate on American jobs lost is underestimated.

Clearly, for a new company to generate such a volume of business indicates the seriousness and aggressiveness with which we opened our doors. With support from the appropriate government officials, this business, we believe, could have been effected. Also, this business would have had a "snowball" effect, increasing the U.S. business presence in an area currently dominated by European or other exporters.

Our Primary Areas of Operation. From its inception, TWP decided to specialize in certain neglected and yet developing markets in Africa, the Middle East and Asia. We firmly believe that foreign aid should be supplanted by facilitation of trade, in line with the old axiom, "Give a man a fish and he eats for one day. Teach a man to fish and he eats for a lifetime." Increasingly, these areas of the world are interested in the free-market system, and TWP is committed to an involvement in this goal.

Unfortunately, we were not able to supply any of the orders for U.S. goods due to the lack of assistance from the EXIM Bank, the FCIA and U.S. banks. Despite the fact that we had discussed the transactions with EXIM before the issuance of the letters of credit to ensure that each LC was issued in accordance with EXIM requirements, we were caught in what we feel was an inefficient, bureaucratic morass. On our first transaction EX-IM delayed the issuance of the necessary coverage to enable the U.S. banks to finance the transaction (the Special Buyers Credit Limit, or "SBCL"). By the time the SBCL was issued, no bank was willing to finance the transaction, including our bankers in Washington, American Security Bank.

On the second transaction, which included the supply of wheat flour for $1,592,500.00 and vegetable oil for $834,865.92, the EXIM refused to even consider our application for the SBCL. Our telephone calls to EXIM officials were seldom returned. We applied to the Foreign Credit Insurance Association ("FCIA") for the issuance of an insurance policy to enable us to complete the transaction. We were declined. We applied again and were declined. (Each application cost us $35.00.) We spoke again with EXIM officials to no avail, and though we presented the orders to several U.S. banks, none was willing to assist us. We were determined to fill the orders and finally restructured the transactions through a Luxembourg bank. We shipped the products through Europe to our buyer.

Our conclusion is this: EXIM Bank and FCIA are only interested in big companies such as Boeing, McDonnell-Douglas and the like. The irony in this is no company gets to be as large as McDonnell-Douglas in one year, and it will require companies like TWP in large numbers to help bring down the trade deficit, broaden the range of markets for U.S. goods, and help create and maintain U.S. agricultural and industrial jobs.

EXIM's attitude toward export trading companies appears to us to be negative, and we believe small exporters will confirm the frustration they face in working with EXIM. Apparently, EXIM's in-house policy is to deal primarily with manufacturers rather than ETCs. Recently we were approached by a palm oil mill to supply machinery and equipment necessary to expand their operation (see enclosed copy of letter of mandate). EXIM again declined to work with us and suggested that the manufacturer apply directly. This supports our conclusion that EXIM does not encourage ETCs. We are currently sourcing the machinery and equipment for this buyer from France. We also are aware of another certified ETC working in the Caribbean which was refused issuance of an EXIM policy as the exporter of record. EXIM preferred to show the manufacturers as exporter of record.

Mr. Chairman, we would make the following recommendations to the Subcommittee to enhance the effectiveness of the ETC Act and the utility of the government bodies charged with facilitating U.S. exports:

1. *EXIM should be mandated to recognize and assist all certified export trading companies, maintain a list of same (and review financial positions if necessary), and set up an in-house system to handle applications*

and inquiries from the ETCs. EXIM's assistance provided to certified ETCs should be a required item for disclosure in its annual report, with particular focus on the number of guarantees issued to ETCs and other facilitation of international trade.

2. ETCs should be directly represented on the Boards of Directors of EXIM and FCIA.

3. ETCs should be issued a general policy by FCIA and EXIM as they are certified with specific commitments and guarantees subject to FCIA or EXIM approval, with the burden of supplying need for denial upon the government agency. Denial of policy approval itself defeats the purposes of the ETC Act.

4. The Commerce Department should enhance its informational efforts, perhaps setting up a clearinghouse for ETCs, banks, manufacturers and other factors in international trade, to help each better understand the importance of the other.

* * *

Chairman Barnard, with the right atmosphere for trading operations in the United States, U.S. products can compete anywhere. One big advantage we as U.S. companies have is that U.S. products often set the world standard for quality. Few would contest this. Where we fall short is in applying our ingenuity fully to create the atmosphere of cooperation among all the actors in U.S. exporting -- manufacturers, trading companies, banks, consultants, political and economic analysts, and government officials.

I hope these comments are useful to the Subcommittee. I am looking forward to its findings.

Very truly yours,

Fred O. Oladeinde
President

FOO/aso
Enclosures

(412) 331-3100

TAYLOR-WILSON MANUFACTURING CO.

THOMPSON AVENUE

MCKEES ROCKS, PENNA. 15136

April 9, 1986

RECEIVED
APR 17 1986
COMMERCE, CONSUMER AND
MONETARY AFFAIRS SUBCOMMITTEE

The Honorable Doug Barnard, Jr., Chairman
Commerce, Consumer, and Monetary Affairs Subcommittee
of the Committee on Government Operations
House of Representatives
Room B377, Rayburn House Office Building
Washington, D.C. 20515

Dear Congressman Barnard:

I am pleased to be given the opportunity to relate to you the experience of Taylor-Wilson Manufacturing Company and its officers in dealing with the Export-Import Bank and the Small Business Administration in processing our application for a guaranteed loan to finance the production of products for export. I will attempt to follow the chronology of your letter of March 26, 1986 in this response, but will omit repeating your inquires. Please corrolate these comments with your letter.

1. Taylor-Wilson Manufacturing Company has been exporting finishing machinery for pipe mills (eg. pipe and tube cut-off machines, hydrostatic testers, automatic coupling screw-on machines, bar and tube straighteners, etc.) for over fifty years. In August, 1984, we concluded contract negotiations with the China Metallurgical Export and Import Corpostion, Beijing, China for the sale of (1) pair of automatic high-speed carbide tool cut-off machines, handling tables, chip conveyors, and crop manipulators to be delivered before mid-August, 1985 for a total-price of $ 1,812,572.00 including spare parts.

2. In early September, 1984, we under the auspices of the Pittsburgh office of the U. S. Department of Commerce, entered into discussions with representatives of the Small Business Administration to negotiate with Mellon

Bank, N.A. a loan in the amount of $ 800,000.00 to be guaranteed 45% by the S.B.A. and 45% by the Ex-Im Bank. A commitment fee of 1/2 of 1% of the principal amount or $ 4,000.00 was submitted through Mellon Bank, on March 20, 1985 but was returned when, as detailed below, we subsequently rejected the loan conditions.

3. Although serious discussions on structuring the loan and meeting documentation requirements began in late October, 1984, formal application was not made until early February, 1985. The preparation of the required corporate financial data was not overly burdensome, but obtaining clarification on the depth of financial disclosure of the officers required considerable discussion and correspondence. The application was approved February 26, 1985, at which time we first learned of the collateral requirements, personal guarantees, restrictions and possible additional costs discussed below.

4. The guarantee commitment fee of 1/2 of 1% was in addition to the interest rate of prime + 3/4 adjusted semi-annually and ---- "any and all expense incurred or which may be thereafter incurred, by the lender from time to time in connection with or by reason of borrower's application for the making and administration of the loan". Since the life of the loan was only six months the real annual cost of borrowing was prime + 1-3/4 plus an unknown expense cost. Quite frankly, Congressman Barnard, considering the collateral requirements and guarantees, we could have gotten better rates from any commercial loan company in the area. These high fees and unknown expenses were very instrumental in our decision not to take down any of this loan.

5. The collateral requirements, made known only after all of the time, effort and expenses had been expended in the preparation of application documents, was in fact a pledge to all of our corporate assets (except realty) that as of December 31, 1984, consisted of $ 3,577.157.00 current assets and $ 173,683.00 of machinery and equipment. This plus the required guarantees of two corporate officers to pledge all of their personal assets would provide collateral in excess of five times the face value of the loan. All of this was to be under first lein recorded in conformity with applicable U.C.C. It was our understanding that this was required by both S.B.A and Ex-Im.

6. We experienced many misgivings relative to some of the five specific conditions and twenty (20) "other provisions" chief of which were:

    1. The effective signing of a blank check to allow the lender to be reimbursed for any expenses he might incur in connection with the loan without any input from the ultimate payor.

    2. The resistriction that any funds from the guaranteed loan not be used to pay any indebtedness incurred prior to approval of the loan even though such indebtedness was incurred on the project for which the guaranteed loan was sought.

    3. The lender may, at its own disgression perform or have performed an audit of the books and records at the borrower's expense. Items of this nature make the total cost of obtaining a guaranteed loan prohibitive.

    The type of documentation such as the requirement that a first lien on all assets other than real property be recorded under U.C.C. and that a mortgagee clause be included in all casualty insurance policies, is normally reserved for long term borrowing, not loans that mature in six months.

7. We had excellent co-operation from every individual representing the S.B.A., the Ex-Im Bank and the Department of Commerce.

8. Based on our experience, the cost, application documentation and post-approval restrictions make this program in its present form, the least desirable method of borrowing. We, after rejecting the approved guarantee from S.B.A. and Ex-Im Bank, arranged for a unsecured line of credit at prime plus 3/4 in the amount of $ 850,000.00, on which we drew a total of $ 575,000.00 over five months and paid the balance in full at the end of the fifth month.

> It is quite obvious that if this program is intended to encourage and assist small manufacturers to expand their export trade, the bureaucratic documentation requirements must be restructured to those used in modern banking and the total borrowing costs musts be made as attractive as the rates that can be obtained from other lending institutions.

Thank you for granting us the opportunity to express our opinions of this program.

Very truly yours,

TAYLOR-WILSON MANUFACTURING COMPANY

Otto F. Kellman
Treasurer

ft

AEGIS

American Export Group
International Services, Inc.

Corporate Headquarters: Watergate 2600
2600 Virginia Avenue, N.W.
Washington, D.C. 20037
United States of America
Telephone (202) 342-0100
Telex: (ITT) 440156 Amex UI
(RCA) 248517 Amex UR
(WUD) 89-639 Amexgroup-Wsh

Writer's Direct Dial No: ____________

RECEIVED
APR 18 1986
COMMERCE, CONSUMER AND
MONETARY AFFAIRS SUBCOMMITTEE

15 April 1986

Hon. Doug Barnard, Jr., Chairman
Commerce, Consumer & Monetary
Affairs Subcommittee
Rayburn House Office Building, Rm B-377
Washington, DC 20515

Dear Congressman Barnard:

This letter responds to your letter dated 26 March 1986 soliciting comments on our experience with the Export-Import Bank's Working Capital Guarantee Program.

Our comments are, by necessity, general in nature, because executives most knowledgeable about our experience are either no longer with AEGIS, or are travelling overseas, and because our application was eventually withdrawn. It apparently foundered on Ex-Im's request for personal guarantees.

Our need for the guarantee program was not to help finance a particular transaction, but rather to guarantee that portion of our general bank line of credit earmarked for issuance of stand-by letters of credit needed for bid and performance guaranties. Thus, goods for a specific transaction were not being purchased with loan proceeds, so normal collateral, i.e. inventory and receivables, would not be available.

The program, as structured, probably works better for guarantees of loans to manufacturing exporters for specific transactions than for guarantees of revolving credit lines to general export trading companies.

We believe that there is a need--as yet unfulfilled--for a program to guarantee stand-by letters of credit issued as bid, advance payment and/or performance guarantees. This need is especially great for trading companies such as ours. The kinds of transactions best handled by trading companies--export of a package of materials--frequently require the exporter to provide the guarantees mentioned. And, since trading companies don't operate from large asset bases, establishing the necessary bank lines of credit can be most difficult. US trading companies could export more if they had large lines of credit earmarked for stand-by letters of credit.

Recipient of the President's "E" Award for Excellence in Exporting

US banks could establish these large lines if a program existed to guarantee the line.

If you would like to discuss this further, please let me know.

Sincerely,

Nelson T. Joyner
Sr. Vice President

TOOLS & MACHINERY BUILDERS INC.
BOX 176 ARCADIA, MISSOURI 63621 PHONE 314-546-3937

May 7, 1986

Mr. Doug Barnard, Jr.
Congress of the United States
Rayburn House Office Building, Room B-377
Washington, DC 20515

RECEIVED
MAY 1 [illegible]
COMMERCE, CONSUMER AND
MONETARY AFFAIRS SUBCOMMITTEE

Dear Mr. Barnard:

Our firm has been contacted by members of your staff regarding our experience with the Export-Import Bank's Working Capital Guarantee Program. Reference your letter of March 26, 1986. I will respond to your questions as follows:

1. Our firm manufactures equipment for the packaging industry with emphasis on Composite Can (i.e., orange juice, snack food, oil) Equipment. Incorporated in the State of Missouri on September 15, 1956. Tools & Machinery Builders, Inc. currently employees 17 people with annual sales of $2,000,000. Export sales as a percentage of total sales for 1984, 1985, and first eight months of 1986 have been 65.3%, 49.5% and 71.0% respectively. Tools & Machinery Builders has aggressively sold in the Export market since 1972. Primary markets were in Canada, Mexico, Taiwan, Japan and Brazil. Only one contract, in 1973, involved Ex-Im Bank financially which was arranged by the Buyer in Brazil and his affiliate in the United States, Container Corporation of America. Tools & Machinery Builders was not involved in the transaction except banking of documents at shipment.

   In early 1983 we submitted to Centerre Bank information regarding a prospective customer in the People's Republic of China. The magnitude of the project if undertaken by our firm would be beyond our current working capital capabilities. It was suggested that we apply for a new program available through the Ex-Im Bank. We provided the necessary documentation i.e. quotations, sales folders, equipment specification and the cost of attending the trade show associated with contract negotiations (copy of these documents enclosed).

COMPLETE COMPOSITE CAN CONSTRUCTION EQUIPMENT

2. A. The dollar amount of the guarantee no. XT-122-1 (see copy of letter dated 9/15/83 enclosed) was $759,000.

   B. Our firm did not pay the Ex-Im fee or accept the loan guarantee or draw down under it. Mr. Fred Zamon's letter dated 9/28/83 to Mr. Kendrick explains the basic reasons our firm did not accept the Ex-Im guarantee.

3. Tools & Machinery Builders was one of the first to apply and be granted an ETC guarantee. Unfortunately the process was not ready for us. Mr. Zamon, in his letter of 9/28/83 planly stated our position "We would like to know what the guarantee says before we pay the fee." The time before application and acceptance was very brief, application, July of 1983 and acceptance September 13, 1983. Unfortunately the receipt of documents did not happen at the same pace. Our firm never received the final documents. Centerre Bank received the draft, over twenty pages in length, several months after the October 13, 1983 due date of the Ex-Im Bank guarantee fee.

4. The fees charged by Ex-Im Bank are shown in their letter of 9/15/83. In addition to the 1.5% of $759,000. our bank had a charge of 1% to administer and establish the guarantee. The total cost would have been $18,225. in addition to the interest computed at prime + 1.25%. Our firm and Centerre Bank felt the fees were high, relative to the benefits afforded under the program. We would have had to assume additional costs of attorney's fees for both Centerre and TMB because the requirements i.e. collateral, restrictions etc. dictated by the guarantee were much different than those used in my line of credit with Centerre.

5. We never received the documents regarding Ex-Im Banks guarantee. Centerre informed us of several problem areas which would cause interference with how TMB's current line of credit was established. In addition there were requirements for key man insurance at additional cost to TMB and personal collateral requirements which I felt would be unacceptable to

myself as major stockholder in the company. The bank would also have to absorb additional costs in administrating the loan because of having to segment the collateral between that associated with the guarantee and other projects in our plant. We are located 100 miles from Centerre Bank. I fully agreed with Centerre's analysis although we did not view the document either in draft or final form.

6. The documentation for approval of the loan guarantee was quite reasonable although I'm not familiar with the documents prepared by the bank. I'm sure that Centerre had most of the information required in their files due to our long term relationship with them. Requirements as indicated in paragraph 5 were mentioned to us by Centerre bank officials after receiving the draft guarantee document. Based upon their analysis we determined that aspects of the contract would cause difficulty with both our firm, me personally and Centerre Bank.

7. Our firm had established a relatively good relationship with Centerre Bank. We are a growing firm entering new markets which required working capital financing. Mr. Zamon from Centerre bank felt the new program may be the right method to solve our problem. Unfortunately the fee structure, contracts and guarantee requirements were not available until after the application was made. Once all of these were received and analyzed it was clear that other less costly and cumbersome methods could be used. We ultimately received additional financing from Centerre using the assignment of proceeds from the People's Republic of China letter of credit. The final contract amounted to $960,000. with $700,000. loaned by Centerre, over and above our current line of credit.

8. I recommend that the fee structure be based on the actual amount used by the borrower rather than the contract amount. In many cases the borrower will not need the full amount of the contract, why have fees on that amount. Most small business exporters like ourselves need a program similar to that offered by Ex-Im Bank's Working Capital Guarantee Program. We

unfortunately have the majority of our current assets and and in some cases personal guarantees established with our current lending institutions. The program should be more flexible to keep from changing the capitalization of the company to comply with the guarantee requirements of the program.

I hope the above information and documents are of help in your examination. I would recommend you contact the following individuals who were greatly involved in our project.

1. Mr. Fred Zamon
   Vice President
   American Security Bank
   1501 Pennsylvania Avenue, N.W.
   Washington, D.C. 20013
   (202) 624-7643

2. Mr. Gary Peterson
   V.P. International Division
   Centerre Bank NA
   One Centerre Plaza
   St. Louis, MO 63101
   (314) 554-7901

Please let me know if we can be of further assistance.

Very truly yours,

TOOLS & MACHINERY BUILDERS, INC.

Stephen E. Owens,
President

SEO/db

enclosures

mTB

TOOLS & MACHINERY BUILDERS INC.
BOX 176 ARCADIA, MISSOURI 63621 PHONE 314-546-3938

QUOTATION

July 27, 1983

Quotation #2124

COPY

Pan China International, Inc. ✓
366 Fifth Avenue, Rm. 1115
New York, NY 10001

Attn: Mr. Ven Wu

Dear Mr. Wu:

It is our pleasure to provide price and delivery information on equipment necessary to manufacture composite cans of 401 diameter. The equipment offered is of TMB manufacture or manufactured to TMB's specifications. Flexibility is built into the system to enable full utilization of all equipment. All equipment is of TMB manufacture unless otherwise specified. The enclosed line layout #TMLL-862 depicts the equipment offered.

Item 1: One (1) TMSW automatic composite can spiral winder with integral electrical panel and Warner Electric motion control system. Unit set up for cutting twelve (12) composite cans per stroke at approximately 32 strokes per minute. The TMSW comes equipped with 20 H.P. drive system, one each water cooled, chrome plated winding mandrel and hardened cutting mandrel. Size determined by customer not to exceed 610 diameter. Maximum paper slit width seven inches.

Power Req: 230/460V, 3 Phase, 50 cycle, 86 amp @ 230V

Air Req: 60 CFM @ 80 PSI

Crate Size: (1) 9' x 4'6" x 5'
(1) 9' x 4'6" x 6'

Net Weight: 10,000 lbs.

COMPLETE COMPOSITE CAN CONSTRUCTION EQUIPMENT

Item 2: One (1) TMGP-3 three tier adhesive unit for applying metered amounts of adhesive to body stock in a spiral winding operation. Each glue unit equipped with all stainless steel adhesive contact components, emersion type adhesive pans with heat regulators and all large 9" wide glue application rolls. Units mounted on common frame.

Power Req: (3) 230/460V, 3 Phase, 50 cycle gear motors
(3) 1000W emersion heaters 110V, 50 cycle, 1 Phase

Air Req: Static only

Crate Size: 10' x 6' x 7'

Net Weight: 4,500 lbs.

Item 3: Two (2) TMSU in-line skiving units. Skivers used to remove outer edge of body ply for stronger can construction. The TMSU is equipped with dual Cincinnati Electric precision spindles and slides mounted with specially designed 5" dia. carbide cutters. Each unit comes prewired with all necessary guides and rollers mounted on common frame. Descriptive information and photos enclosed.

Item 4: Three (3) TMIF individual body ply festoons for use in the manufacture of spirally wound composite cans. Each unit designed for use with 3" diameter inside, uncored rolls with an outside diameter of up to 60". Festoon rollers a full 13'6" high with double accumulator roll bracket counter balanced for tension while making splice, triple roll on bottom giving operator five full wraps.

Item 5: One (1) TMLS liner stand for use in guiding, lubricating, impregnating with glue and adhering inner body liner to a composite can. Consists of the following items:

(1) single "Fife" guide unit
(1) TMIF-L liner festoon
(1) Anaconda fold unit
(1) edge fold glue unit
(1) mandrel lubrication system
(1) heatseal unit with controller
(2) Warner tension control devices

All of the above items mounted on common frame to TMSW, item one.

Item 5: (Continued)

Power Req: 1/2 H.P., 220/440/3Ph., 50 hydraulic motors
1/4 H.P., 220/440/3Ph., 50 gear motors, 2000W
220/1Ph./50 heater element

Air Req: None

Crate Size: (1) 9' x 4' x 5'

Net Weight: 1,400 lbs.

Item 6: One (1) TMGP-L label glue unit with label festoon. Glue system same as that offered under item two, but includes photo eye for label registration system. Unit includes festoon equipped with dual roll spindles each with Warner tension control. Torque assist drive feature decreases the amount of tension required to drive glue roll.

Power Req: (1) 1/4 H.P., 230/460V/3Ph/50 gear motor
(1) 1/8 H.P., 230/460V/3Ph/50

Air Req: Static only

Crate Size: (1) 8' x 4' x 5'

Net Weight: 2,200 lbs.

Item 7: One (1) TMVF-6 automatic vertical flanger. Designed specifically for use in the composite can industry. The TMVF-6 has a diameter range of 202 through 610 and a height range of 200 through 1200. Special units can be designed upon your specific requirements. The movable top flanging head and worm infeed bracket are the only items required to adjust can height on the TMVF-6 while maintaining a 34" can infeed height. The TMVF-6 unit is capable of speeds in excess of 300 cans per minute.

Item 8: One (1) Angelus 60L Sanitary Can automatic can manufacturing seamer. Supplied with 401 x 514 change parts, automatic jam stop control system, worm type can feed, seaming chucks with arc deposited carbide surface, variable speed motor drive, and extended cover feed chute with 60" trough, electric vibrator and bent stack rods for 401 can diameter.

Item 9: (A) One (1) 19'0" long take-a-way conveyor three speed, with good & bad pneumatic discharge gates.

(B) One (1) fully adjustable can upender. Approximate length of 2'6".

(C) One (1) table top chain conveyor 54'0" with short discharge conveyor from upender into seamer.

(D) One (1) 8'0" x 16'0" bi-directional accumulating table.

(E) One (1) table top chain conveyor 12'0" with guides to transfer cans from items "C" and "D".

(F) One (1) table top chain conveyor total length approx. 12'9" with 90° turn and infeed into can cleaner (item 10), chain width 6", infeed into twister and discharge into vertical elevator.

(G) One (1) fully adjustable vertical double belt can elevator with discharge height of approximately 14'0".

Item 10: One (1) ionized air can cleaner. Rotational Brush at infeed end. "V" belt side drive system to convey containers through system by spinning action. Removes static charged particles from inside of container.

Item 11: One (1) cable track conveying system for transporting containers to palletizing area. System must be designed for each plant installation. Price includes 300' of cable track section in 10'0" lengths, one drive section, one take-up section, one 180° return section and two (2) 90° sections with all WIRELON (coated) and hangers based upon 20'0" ceiling height and 12'6" cable height. Each system includes gates required for transfer onto palletizer, item 12.

Item 12: One (1) empty can palletizer model R802 with the following features:

- 21'0" accumulating table
- Semi-automatic controls
- Chipboard rack
- Powered chipboard gripper
- 54" wide operator platform with stairs
- Model MA50 automatic pallet dispenser
- Soft start on all pallet motors
- Automatic layer squaring
- Automatic pallet discharge 7'0"
- 110" Pack height

Item 13: One (1) Application Engineering Corp. portable water chiller. Model No. DSA-5. Unit used for chilling the winding mandrels on both spiral winders, item 1. System is completely recirculating.

Item 14: One (1) Steelcraft Corporation Dust Collection system for use in handling, collecting, and compacting paper dust from a skiver operation. Includes the following major components:

(1) 6'0" H.S.L.C. collector
(1) Maren #14 high density dust baler
(1) #915 paper dust handling blower
(1) 25 H.P. 1800 RPM motor
(1) Belt drive and guard
(2) 6" rubber (Flexhaust) clean ups
(1) Lot of pipe, fittings, connections, flanges to install dust system
(1) Bloapco chopper unit

Power Req: 230/460V, 3 Phase, 50 cycle

Air Req: Static air clutch

Crate Size: 7'6" x 4'7"

Net Weight: 3,000 lbs.

QUOTATION

Item 15: Air Compressor system with refrigerated air dryer, holding tank. Components are as follows:

1 each - Model GAU607 60 H.P. air cooled rotary screw air compressor. Unit rated for 280 C.F.M. at 100 PSI. Comes complete with acoustical enclosure, air cooled after cooler and moisture seperator, motor starter, automatic on-off control, high air/oil temperature shutdown switch and control and monitoring panel. Unit manufactured in Holyche, MA.

1 each - Model R250A refrigerated air dryer designed to provide a 35°F. dewpoint for 250 C.F.M. and a 50°F. dewpoint for 300 C.F.M. Unit manufactured in Ceinton, MI.

1 each - 300 gal. holding tank

Item 16: One (1) Quality Control package including the following items:

- (1) TMI H & D crush tester
- (1) TMI model 590 thickness guage
- (1) can height guage
- (1) internal pressure tester
- (1) water pressure test for seam integrity
- (1) slip & friction tester for coefficient of friction test on materials
- (1) Double cut seamer saw
- (1) curl & seam diameter "GO" & "NO GO" guages
- (1) 1000G digital scale

Item 17: One (1) Model M-1730 Hydraulic tilters for use in upending rolls of paper on a pallet. The load deck is 52" x 52" and 24" above floor. The unload forks are 6" wide x 60" long and when tilted 90°, lay directly on the floor. Unit capacity is 4,500 lbs. Each tilter is equipped with a self-contained 1-1/2 H.P. power unit completely wired and requiring one point power connection (460V/3 Phase/50 HZ). A two button push button control and 10' flexible cord are included for field mounting as required.

mTB

Item 18: Electrical control panel for all can handling and line control devices.

Item 19: One (1) training program consisting of the following:

A. Three (3) week training period for four (4) personnel and one (1) supervisor. Recommend that mechanic, electrician and two operators participate. Consists of in class and hands on experience.

B. Two (2) full sets of training, maintenance and operational manuals.

C. Plant tour to two (2) composite can manufacturing facilities in the U.S.A.

Item 20: Pre-engineering and start-up assistance:

A. Upon acceptance of contract, TMB representative will be available for ONE WEEK of consultation regarding plant evaluation, material specifications, container evaluation and specifications. Based upon data prepared from this evaluation a complete set of equipment and material specifications will be prepared.

B. After installation of equipment, a TMB engineer will be made available for a TWO WEEK start up period.

Total price of the preceeding system Ex Works, Point of Manufacture . .
----------------------$803,000.

Item 21: Estimated inland freight, containerization, insurance and document charges at port.
----------------------$ 25,000.

Total cost of all equipment F.O.B. Port of Export -----$828,000.

DELIVERY:

1. Delivery of the preceeding equipment five months upon receipt of purchase order, one-third deposit, all tooling information and letter of credit for balance.

2. The schedule is dependent upon starting activities at quotation date. If this proposal is not executed within 90 days from the quotation date, it may not be possible to meet the stated schedule. Since this schedule was developed based upon shop loading and other data dependent upon commencing activities, receipt of order past the above time may result in a greater delay in your delivery.

3. If the performance of any part of this contract by seller is prevented, hindered, delayed or otherwise made impracticable by reason of any strike, flood, riot, fire, explosion, war, unavailability of materials and/or supplies, or any other casualty or any other cause of whatever nature that is beyond the reasonable seller and which cannot be overcome by reasonable diligence and without unusual expense, seller shall be excused from such performance during the continuance of any such happening or event and for so long as such event shall continue to prevent, hinder or delay such performance. This contract shall be deemed suspended so long as and to the extent that any such cause shall operate to prevent, hinder or delay performance by seller of its obligations.

PAYMENT TERMS: This quotation is based upon the following payment terms and any deviations could cause price adjustments.

1. A payment of one-third purchase price is to be made with the placement of the order and will be credited to invoices issued under the contract.

2. Balance of payment shall be arranged through letter of credit established with a U.S. bank, preferrably the Centerre Bank of St. Louis. Letter of credit should allow for partial shipments. Funds should be released from the letter of credit upon TMB presenting shipping documents to the bank. Under no circumstances will TMB release title to any merchandise quoted herein until the total contract price has been paid in full.

3. If the buyer fails to pay the price as it becomes due, the seller may recover together with any incidental damages and its costs of collection, including a reasonable attorney's fee, the price of the goods agreed to be paid by buyer plus interest at the rate of 1-1/2% per month on the full amount of the purchaser's price.

GENERAL TERMS:

1. To realize the expected results desired of equipment, Purchaser should establish the proper climate for the initial and continuing acceptance of the system by his operating, supervisory and maintenance personnel. The supervisory staff should be advised of the proper blending of reliable equipment, adequate supervision and sufficient training of operating and maintenance personnel, which will accelerate the achievement of the expected results.

2. All materials shall be constructed in accordance with specifications of Purchaser if furnished in writing. In the absence of written specifications, our own construction standards (standard duty) apply unless otherwise specified herein.

3. All electrical equipment, unless otherwise requested, will be wired 230/460/3Ph/50 cycle consisting of TEFC motors and "Allen Bradley" starters and controls.

4. Unless otherwise specified, all non-machined surfaces will be painted Vista Green machine enamel as manufactured by Pittsburgh Paint Company.

5. TMB has made every reasonable effort to design and specify the equipment described in this contract in accordance with the Williams-Steiger Occupational Safety & Health Act of 1970 (OSHA), insofar as our understanding and interpretation of the Act permits. TMB, therefore, does not guarantee that any equipment furnished under the terms of this contract meets the Act in all respects nor does TMB agree to indemnify and hold harmless the Purchaser from any costs, direct or consequential, fines or assessments resulting from failure of items covered under this contract to comply with the provisions of OSHA.

QUOTATION

6. TMB WARRANTY-LIABILITY TO OUR CUSTOMERS IS INDICATED IN PARAGRAPH FIVE (5) ON THE REVERSE SIDE OF THIS QUOTATION.

7. This Proposal shall be interpreted and enforced in accordance with the laws of the State of Missouri.

8. This quotation enters into contractual effect when signed by duly authorized representative of Purchaser and of TMB. This quotation may not be modified or rescinded except by the written agreement of Purchaser and TMB.

APPROVED AND EXECUTED BY:

PAN CHINA INT., INC.	TOOLS & MACHINERY BUILDERS, INC.
By__________ Signature	By__________ Charles T. Chan
Title__________	Title V.P. of Sales
Date__________	Date July 27, 1983

mTB

EXPORT-IMPORT BANK OF THE UNITED STATES
WASHINGTON, D.C. 20571

CABLE ADDRESS "EXIMBANK"
TELEX WU 89-461
RCA 248460

September 15, 1983

COPY

Centerre Bank N.A.
One Centerre Plaza
St. Louis, MO 63101

Attention: Frederick J. Zamon
Vice President

Re: Export Trading Company Loan Guarantee No. XT-122-1
Borrower: Tools and Machinery Builders, Inc., Arcadia, MD
Guarantor: Stephen Owens, Arcadia, MD

Gentlemen:

We are pleased to advise you that the Export-Import Bank of the United States (Eximbank) has approved an Export Trading Company Loan Guarantee (ETC) in connection with your financing of a working capital loan to Tools and Machinery Builders, Inc (TMB).

The ETC has been provided to support the manufacture of an assembly line for the manufacture of composite cans on the following major terms and conditions:

Foreign Obligor:	China National Packaging Corporation, Beijing, China
Guarantor:	Stephen Owens, President and Treasurer of TMB
Amount of Loan:	$759,000.00
Eximbank Liability:	$683,100.00 (90%)
Term of Repayment:	Up to 360 days at Prime + 1.25%
Availability Date:	September 30, 1984
Eximbank Guarantee Fee:	1.5% of the loan amount (due within 30 days from September 13, 1983, date of Eximbank authorization).
Interest Coverage:	Interest accrued to the due dates of the obligation(s) at the rate of the lesser of (i) one percent in excess of the U.S. Treasury borrowing rate for borrowings having the same maturity as the remaining repayment term of the obligation or (ii) such rate as may be borne by the obligation(s).

Security: (1) The loan will be secured by the wholesale value of inventory of exportable goods equal to 110% of the outstanding loan balance.

(2) TMB will assign to Centerre Bank and Eximbank the proceeds of the Bank of China, Beijing, China, Irrevocable Letter of Credit.

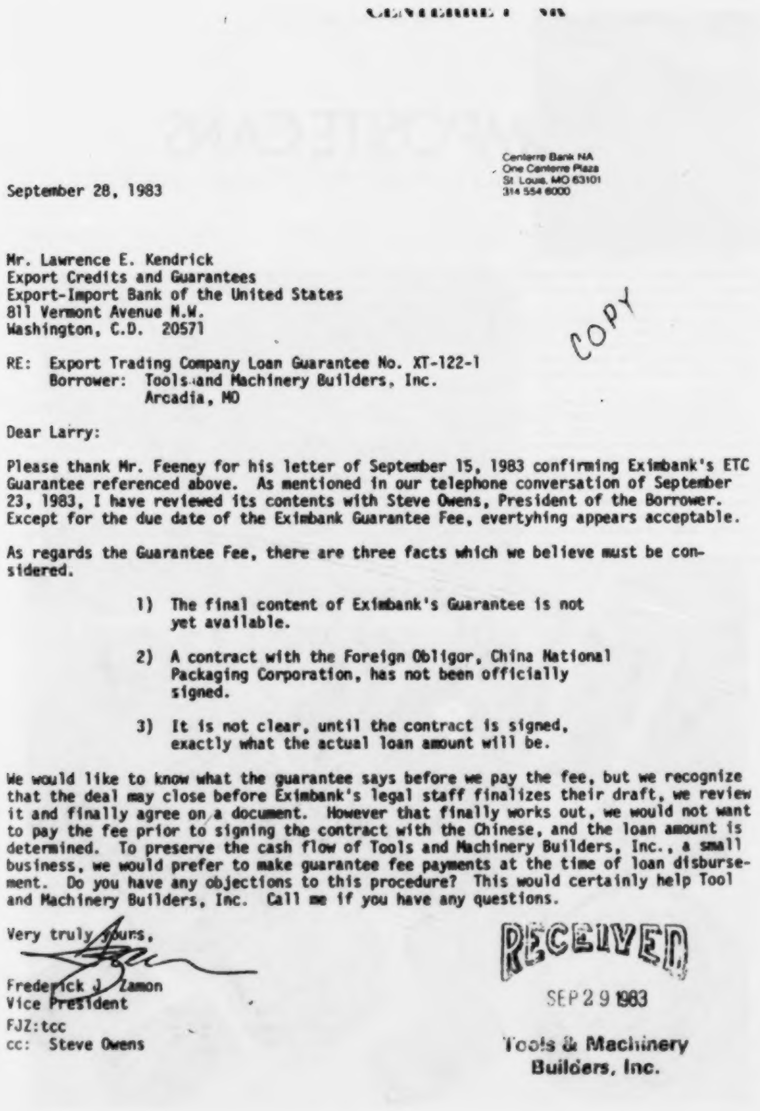
Upon shipment, Centerre Bank and Eximbank will release TMB from the security arrangement in item (1) and will revert to the security arrangement in item (2).

In the near future a Loan Guarantee Agreement setting forth the terms and conditions of the subject Guarantee will be prepared and forwarded to you. Should you have any questions relating to the transaction, please contact Mr. Lawrence E. Kendrick of our staff at 202-566-8347.

Sincerely,

Richard J. Feeney

Richard J. Feeney
Deputy Vice President
Exporter Credits & Guarantees



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Centerre Bank NA
One Centerre Plaza
St. Louis, MO 63101
314 554 6000

September 28, 1983

Mr. Lawrence E. Kendrick
Export Credits and Guarantees
Export-Import Bank of the United States
811 Vermont Avenue N.W.
Washington, C.D. 20571

COPY

RE: Export Trading Company Loan Guarantee No. XT-122-1
Borrower: Tools and Machinery Builders, Inc.
Arcadia, MO

Dear Larry:

Please thank Mr. Feeney for his letter of September 15, 1983 confirming Eximbank's ETC Guarantee referenced above. As mentioned in our telephone conversation of September 23, 1983, I have reviewed its contents with Steve Owens, President of the Borrower. Except for the due date of the Eximbank Guarantee Fee, evertyhing appears acceptable.

As regards the Guarantee Fee, there are three facts which we believe must be considered.

1) The final content of Eximbank's Guarantee is not yet available.
2) A contract with the Foreign Obligor, China National Packaging Corporation, has not been officially signed.
3) It is not clear, until the contract is signed, exactly what the actual loan amount will be.

We would like to know what the guarantee says before we pay the fee, but we recognize that the deal may close before Eximbank's legal staff finalizes their draft, we review it and finally agree on a document. However that finally works out, we would not want to pay the fee prior to signing the contract with the Chinese, and the loan amount is determined. To preserve the cash flow of Tools and Machinery Builders, Inc., a small business, we would prefer to make guarantee fee payments at the time of loan disbursement. Do you have any objections to this procedure? This would certainly help Tool and Machinery Builders, Inc. Call me if you have any questions.

Very truly yours,

Frederick J. Zamon
Vice President

FJZ:tcc
cc: Steve Owens

RECEIVED
SEP 29 1983
Tools & Machinery
Builders, Inc.

COMPOSITE CANS

are now a logical choice for diverse products

Rarely does a packaging mode dictate the very existence of a product. Composite cans, however, have done that at least twice—once for refrigerated dough products, and once again for certain snack foods.

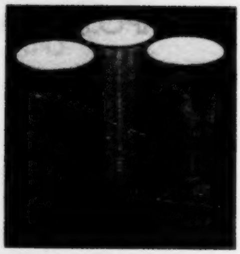
The former, especially, demonstrates some of the design and structural capabilities of a process which dates back to pre-Civil War days, but which has come into its own only since the mid-'50s.

Refrigerated dough products literally would not exist without composite cans because no other packaging method works. The product requires a structurally sound package which can be easily opened in its entirety. The package must display good moisture and gas barrier properties, and be able to withstand internal pressures without failing. And, of course, it must be economically viable. No other packaging mode meets all these criteria.

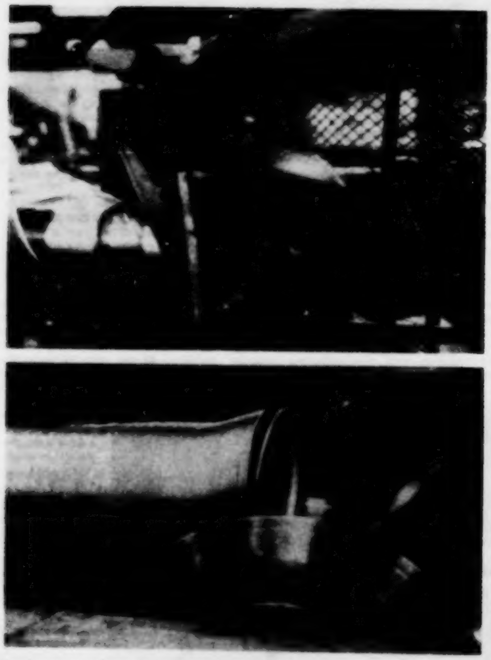
The snack food revolution is a less clear cut example. Other packaging modes do exist—although they are, perhaps, not as economically sound—for the snack foods which are being packed in composite cans in ever increasing numbers. Thus, it is conceivable that the first such product—a potato chip-like snack called Pringles—could have been introduced without composite cans. The hermetically sealable composite, though, was the most cost effective package. The cost elements, combined with marketing desires to have a totally new package to go with a totally new product almost dictated that composite cans be the choice. And that choice changed the course of an entire industry.

Historically, snack food was (and mostly still is) essentially a local industry. Even so-called national brands operate with numerous regional producers. Reason: Snack foods in cellophane or polyolefin materials have a shelf life of about 30 days. The packer, in his rounds, removes any product older than that and replaces it with fresh goods. Switching to a nitrogen flushed composite can extends shelf life to at least one year. This makes national distribution through regular channels possible.

These two products also demonstrate another facet of the composite can industry—one of particular importance to packaging decision makers. Technological developments tend to take quantum leaps, rather than following a steady developmental trend line. Thus, rapid advances in liner and labeling



Right: A comparatively recent technique is to convolute wind a label onto a spiral wound can. This results in the structural advantages of a spiral can, while allowing short runs. For instance, Clevepak used this technique for Borden's so it could test market three different sets of graphics on its Cremora coffee creamer.



Spiral winding produces a composite can of exceptional structural integrity, including specific barrier properties as required. Essentially a continuous process, rolls of body material revolve diagonally around a stationary mandrel (top). After being cut to size, tops are attached (bottom).

technology led to the refrigerated dough products of the '50s; new body wall technology saw the introduction of composite motor oil cans in the '60s, and liner, body materials, labeling, and closure technology led to the hermetic sealing and easy openability which made the snack food revolution of the '70s possible.

Hence, if you haven't checked out composite containers recently because you think them unsuitable for your products, it may be time for another look-see, especially if you package food products, many of which could not be packed in composite cans as little as two or three years ago, but which now are commonly packed that way. One example is the peanut butter can, introduced recently. What's more, the next R&D round will see capabilities undreamed of five years ago.

Despite these rapid changes, the basic composite container processes haven't changed much in over 100 years. One of two winding methods, either spiral or convolute, is used to wrap layers of body material around a metal mandrel. This produces a composite tube, to which a top is attached. The user fills the container on regular filling equipment, and attaches the bottom. The only differences between a tube, can, or drum are size and kind of closure.

Spiral wound containers are the most common. These are made continuously by winding body materials at an angle around a stationary mandrel. The outermost layer—of paper, foil, polyethylene, or a co-extrusion, forms the label, and the innermost layer is the liner. Each layer picks up adhesive as it winds, and the whole forms a continous tube which is cut off to proper length. This is a fast, economical process that produces a can of exceptional structural integrity which can be tailor made for any combination of barrier characteristics.

Convolute winding consists of a revolving mandrel which pulls body material around itself. It is a non-continuous system that relies on a series of timed, intermittent processes. Typically, convolute containers do not have liners, nor does the can have as

COMPOSITE CANS

high a level of structrual integrity as spiral winding. But convolute cans can be made into shapes other than round, and are ideal for built-in easy openers, such as string pulls. Convolute winding is a relatively slower, less economical process, but it is good for short runs, or for constructing a customized package.

Although the basic process has not changed, the technology of producing today's composite can has. It's a rare can, for instance, that is made of fibreboard only. By and large as C. Mack Gavitt, vice president-manufacturing for Clevepak points out, fibreboard not only provides structural strength, but is used as a carrier of other, barrier property materials.

Instead of a straight fibreboard can, modern composites are laminates of fibreboard, foil, and various plastics. The specific combination of materials used depends on the barrier properties needed. Indeed, today's composite can makers have reached the point where they even use co-extruded materials for body walls. Perhaps more than anything else, the use of new materials has been responsible for making composite cans into a natural choice for many products—especially moist, liquid, or greasy materials. As Ben Ruf, national sales manager of CCA's composite can divison, says, "The fact that the industry has learned to run combination materials at good production speeds with a high AQL (acceptable quality level) that are gas tight has enabled us to do a lot of things differently so far as new products go."

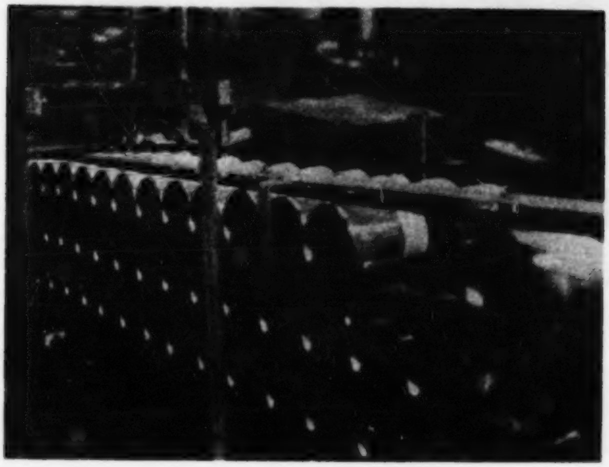
Nor has technological progress been confined to body wall construction. Closure development, too, has taken the same sort of quantum leaps forward. Latest on the scene are membrane closures. These thermoplastic/foil/thermoplastic, or thermoplastic/foil/fiber/thermoplastic laminates are fast replacing easy-open metal tops—themselves a fairly recent introduction.

The membrane or peelable seals offer a number of advantages. (1) They are less expensive to buy, (2) they provide a safe edge on both the closure, once it's removed, and on the can itself. Heat sealed to the can, as a primary seal, a polyethylene snap-on overcap is provided for resealability of the can. Among entries so far are Sonoco's Safe-top and Clevepak's Cleveseal.

Virtually every major producer of composite cans will be offering a membrane closure if for no other reason than consumer and regulatory agency acceptance is so good. But their use does require a slightly different approach on the filling line.

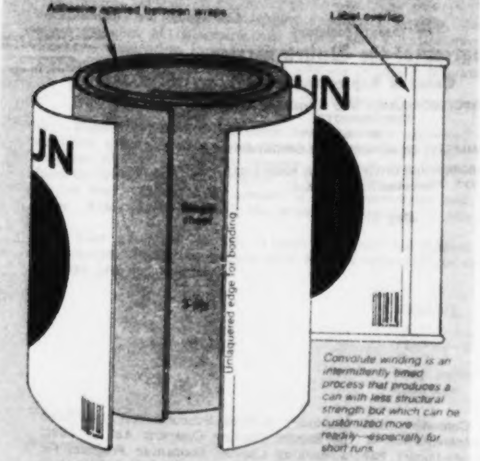
Normally, composite cans are supplied with the tops in place. After filling, the user attaches the bottom. Anyone ordering cans with membrane closures is likely to find the opposite situation, because:

- Many composite can makers think that packaging product against the membrane is not too good an idea. This especially is true with hot-fill products, because there's a danger that the gas tightness of the membrane heat seal could be adversely affected.
- Run speeds for attaching membrane seals are considerably slower than can makers can easily tolerate. Can making lines can be slowed by as much as 40 per cent. Because filling lines normally run slower anyway, it



and the finished cans are inspected automatically, then stacked awaiting packing and shipment to customers. Spiral winding accounts for the vast majority (probably in excess of 95 per cent) of the composite cans used

COMPOSITE CANS



Convolute winding is an intermittently timed process that produces a can with less structural strength but which can be customized more readily—especially for short runs.

Convolute wound composite can

makes more economic sense for the packer to attach the ends.

What's coming? Composite can makers are looking ahead to breakthroughs that will allow high pressure, hot filled products, and carbonated beverages to be packed in composite cans. Admittedly, these developments are far downstream—some estimates put it at five to ten years at the earliest. But the technology for many of these—especially in the areas of high pressure—already exists on a laboratory scale. As one industry leader notes, "The only stumbling block remaining is to bring the costs down to a competitive level."

For packaging users, that's a key issue. And it's one that impacts as much on supply as it does on price. The aborted coffee can amply demonstrates the problem. After years of R&D and considerable capital outlay (amounting to more than $1 million for just one company), the industry introduced a composite can for coffee. Immediate acceptance of the can was widespread. But metal coffee cans are a big business, and one that producers are reluctant to lose any share of. Suddenly, the price of metal coffee can stock plummeted, making the composite can non-competitive and it was withdrawn.

Could this happen again with new cans? According to composite manufacturers, the price differential between composites and competing materials is too large now, and is growing at too accelerated a rate for that ever to happen again. And the applications they are looking at—pressurized tennis balls on one hand, and carbonated beverages on the other—are large enough to be worth grabbing any size share of market. Whether competing containers makers will retaliate or not, therefore, is a question that will be answered only when the composite makers solve the technological and economic problems remaining. In either case, user choice will likely be determined by that answer.

Another clue to where composites are going lies in a totally different direction. Anything that requires retorting, of course, cannot be packed in a composite can. But new developments in aseptic packaging—especially in areas like chemical pasturization—have the industry very excited. "We can expect," stresses one spokesman, "to capture a diversity of products as aseptic packaging technology advances."

■

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C. THE SUBCOMMITTEE'S MAY 1986 LETTER TO EXIMBANK AND THE BANK'S JUNE 1986 RESPONSE AND OTHER INFORMATION

DOUG BARNARD, JR., GEORGIA, CHAIRMAN
JOHN M. SPRATT, JR., SOUTH CAROLINA
JOE KOLTER, PENNSYLVANIA
BEN ERDREICH, ALABAMA
ALBERT G. BUSTAMANTE, TEXAS

NINETY-NINTH CONGRESS
Congress of the United States
House of Representatives
COMMERCE, CONSUMER, AND MONETARY AFFAIRS SUBCOMMITTEE
OF THE
COMMITTEE ON GOVERNMENT OPERATIONS
RAYBURN HOUSE OFFICE BUILDING, ROOM B-377
WASHINGTON, DC 20515

LARRY E. CRAIG, IDAHO
PATRICK L. SWINDALL, GEORGIA
H. JAMES SAXTON, NEW JERSEY

MAJORITY—(202) 225-4407

May 6, 1986

Hon. John A. Bohn, Jr.
President
Export-Import Bank
of the United States
811 Vermont Ave., N.W.
Washington, D.C. 20571

Dear Mr. Bohn:

The House Commerce, Consumer, and Monetary Affairs Subcommittee has been examining the impact and implementation of the Export Trading Company Act of 1982, presently focusing on the Export-Import Bank's Working Capital Guarantee Program for exporters and export trading companies. The subcommittee has developed information which requires Eximbank's response for the subcommittee's record. Please respond to the following questions and requests for information, no later than May 22, 1986:

A. Discrepancies in previous data provided to the subcommittee

Subcommittee staff contacted 10 U.S. exporters/trading companies listed on Eximbank's list of "Working Capital Guarantees Issued from the Inception of the Program through February 7 [1986]". Of these 10 entities, listed by Exim as recipients, only 5 actually paid the Exim guarantee fee and obtained a loan covered by it. If Exim's list is not corrected and revised, its inclusion in the record will leave a highly inaccurate and misleading picture of the actual number and amounts of Exim loan guarantees. Therefore, please furnish a revised list showing for each exporter or trading company whose name is on the present list, the following additional information: (1) the status of the guarantee, (2) whether the recipient paid the fee and whether the guarantee was finalized, (3) and the amount of money drawn down on the loan which was guaranteed.

B. Complaints about and alleged problems with the Working Capital Guarantee Program

Howard Hammonds, the president of International Marketing & Procurement Services, Inc., now in bankruptcy, testified before the subcommittee about serious problems with the program (his testimony is enclosed; also, he is listed as a recipient of the guarantee, although he, like others, never utilized it). In addition, several of the "recipients" contacted by the subcommittee voiced complaints about the program, and a few sent letters to the subcommittee (enclosed) describing their particular problems.

Please respond to their allegations (also made by other "recipients" over the telephone to subcommittee staff), addressing the following issues: Exim's routine demand for allegedly "unreasonable" collateral (including personal homes and previously collateralized accounts receivables), the delays and lengthy application process, the continued requests for and large amounts of documentation, Exim's administrative requirements or loan conditions (such as monitoring inventory, receiving invoices, etc.), and the inability to guarantee standby letters of credit issued as advance payment, bid, and/or performance guarantees.

C. Amount of funds allocated to the Working Capital Guarantee Program

Please indicate if Eximbank has separately allocated funds to this program or, if not, how and in what amount Exim apportions funds from other programs. If there is a separate allocation for this program, set forth the following data for each fiscal year, from the inception of the program to the present: (1) the Exim allocation at the beginning of the year, (2) the total amount of final guarantees, and (3) the amounts drawn down upon. Also, please indicate the proposed allocation, if one exists, for FY 1987.

Your attention to this request and your anticipated cooperation are very much appreciated. Please have Exim staff contact subcommittee counsel Stephen R. McSpadden if there are any questions.

Sincerely,

Doug Barnard, Jr.
Chairman

DB:srm:v

Enclosures

EXPORT-IMPORT BANK OF THE UNITED STATES

BORROWERS USING THE WORKING CAPITAL PROGRAM FROM THE INCEPTION OF THE PROGRAM THROUGH FEBRUARY 7, 1986
(Pursuant to P.L. 97-290; October 8, 1982)

This listing provides the borrower, address, person to contact and telephone number of companies that have used the Working Capital Guarantee program.

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BORROWERS USING THE WORKING CAPITAL GUARANTEE PROGRAM SINCE INCEPTION OF THE PROGRAM

BORROWER	STREET	CITY	ST	ZIP	PERSON TO CONTACT	TELEPHONE NUMBER
AEROTECH WORLD TRADE CORP	NEW KING STREET	WHITE PLAINS	NY	10604	ENDRESEN, BERGTHOS, PRES.	914-428-3500
AMERICAN EXPORT GROUP INTL SVCS INC	2600 VIRGINIA AVE	WASHINGTON	DC	20037	FAROUKI, A. HUDA	202-342-0100
BRETTRAGER MANUFACTURING CO.	5410 EAST ROAD	SAGINAW	MI	48601	CLAGETT, THOMAS	517-777-1440
COMTEC ECONOMATION INC	3300 E SPARROW AVE	FLAGSTAFF	AZ	86001	BEAVER, MARY & WILLIAM	602-526-4123
CUMBERLAND HARDWOODS INC	P O BOX 6368	SPARTA	TN	38583	KIESLING, JOHN, PRESIDENT	615-738-5264
DAVIS & BARRYMAN INTERNATIONAL	108 MARION ST N E	RUSSELLVILLE	AL	35653	DAVIS, ROY, PRES	205-332-9164
DCR INTERNATIONAL	29350 SOUTHFIELD ROAD	SOUTHFIELD	MI	48076	PIETRANGELI, ROMULO	313-557-9222
DELTA BRANDS INC	2204 CENTURY CENTER BLVD	IRVING	TX	75062	SAVARIEGO, SAM PRES	214-438-7150
DYNEQUIP, INC.	310 SNELLING AVE NORTH	ST. PAUL	MN	55104	FLAA, DON OR ANDERSON, VINCE	612-645-0979
EDUCATIONAL INNOVATION SYSTEMS INC	394 NORTH LAKE SHORE DR	FONTANA	WI	53125	TURNER, WILLIAM OR BARBARA	414-275-6151
EXPORT MGMT INTL INC	220 E. MADISON ST, #1010	TAMPA	FL	33602	MOISA, JULIO E	813-229-7744
FREMONT GROUP, LTD.	175 NORTH FRANKLIN STREET	CHICAGO	IL	60606	WOLF, DAVID	312-332-4096

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BORROWERS USING THE WORKING CAPITAL GUARANTEE PROGRAM SINCE INCEPTION OF THE PROGRAM

BORROWER	STREET	CITY	ST	ZIP	PERSON TO CONTACT	TELEPHONE NUMBER
GENERAL ROBOTICS CORP	57 NORTH MAIN STREET	HARTFORD	WI	53027	PICK, CARL	414-673-6800
GREAT WESTERN MEAT CO.	P O BOX 915	MORTON	TX	79346	ANOLABAHERE, BEN J., PRES	806-525-4221
HETTINGA EQUIPMENT INC	2123 NW 111TH ST	DES MOINES	IA	50322	HETTINGA, SIEBOLT	515-270-6900
IBBERSON INTERNATIONAL INC	3424 WOODDALE PLACE	MINNEAPOLIS	MN	55416	RASMUSSEN, DUANE	612-929-1641
INTER-CONTINENTAL CONSULTANTS INC	1700 NORTH MOORE AVE	ARLINGTON	VA	22209	PHILLIPS, RUFUS C	703-522-4046
INTERNATIONAL CHIP & ASSOCIATES INC	1 RIVERWAY	HOUSTON	TX	77056	MCQUEEN, CHARLES M	713-552-0412
INTL MKT & PROCUREMENT SVCS INC	P O BOX 1977	BUTLER	PA	15222	HAMMONDS, HOWARD	412-282-2583
J & M DISTRIBUTING CO., INC.	8420 HALL ROAD	UTICA	MI	48087	LAPJI, MASINH M, PRESIDENT	313-642-2773
J & M EXPORT, INC.	10537 14TH AVE S	SEATTLE	WA	98111	DEOLIVEIRA, MARCO	206-242-2341
JERNIGAN TRADING COMPANY INC	9500 BRIARWOOD BLVD	KNOXVILLE	TN	37923	JERNIGAN, VICTOR	615-693-5441
KLUMB LUMBER COMPANY INC	P O BOX 550	CRYSTAL SPRINGS	MS	39059	FIELDS, MARK, TREASURER	601-878-2581
LIVERNOIS ENGINEERING COMPANY INC	25315 KEAN	DEARBORN	MI	48124	WALLIS, B.J., PRESIDENT	313-278-0200

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BORROWERS USING THE WORKING CAPITAL GUARANTEE PROGRAM SINCE INCEPTION OF THE PROGRAM

BORROWER	STREET	CITY	ST	ZIP	PERSON TO CONTACT	TELEPHONE NUMBER
LOOPCO INDUSTRIES, INC.	1981 E AURORA ROAD	TWINSBURG	OH	44087	WITHROW, SUSAN OR DAVID	216-425-7851
MONARCH METALS CORPORATION	430 EAST 86TH STREET	NEW YORK	NY	10028	NADLER, LEE PRESIDENT	212-988-6960
NORTH ATLANTIC TIMBER & SHIPPING	OLD FURNACE ROAD	HARDWICK	MA	1038	VILLA, MARC R	413-477-8862
PETRO CHEMICAL SUPPLIERS, INC	# 2 N SAMPSON	HOUSTON	TX	77001	ROSENSTEIN, THOMAS	713-224-5841
PHILIPPI HAGENBUCH, INC.	7254 W PLANK ROAD	PEORIA	IL	61604	HAGENBUCH, LEROY	309-697-9200
PLATTCO CORPORATION	18 WHITE STREET	PLATTSBURGH	NY	12901	GUIBORD, RICHARD C	518-563-4640
R D SYSTEMS INC	13628 METRIC ROAD	ROSCOE	IL	61073	RIBURDY, JIM	815-389-4559
RAMCO INC	10975 TORREYANA RD	SAN DIEGO	CA	92121	MCCORMACK, DICK	619-452-5963
RESORCON, INC.	12 FEDERAL DRIVE	PITTSBURGH	PA	15235	MCGUIRE, TERRANCE	412-241-5900
RET CORPORATION	6551 LOISDALE COURT	SPRINGFIELD	VA	22150	TRUFFAT, RAUL E	703-922-9713
ROSCOR CORP	1061 FEEHANVILLE DRIVE	MOUNT PROSPECT	IL	60056	ROSTON, MITCH	312-539-7700
SAXON EXPORT CORPORATION	4360 NW 135 ST	MIAMI	FL	33054	ORTEGA, WALTER ABBATE, FLORIO	305-688-1181

BORROWERS USING THE WORKING CAPITAL GUARANTEE PROGRAM SINCE INCEPTION OF THE PROGRAM

BORROWER	STREET	CITY	ST	ZIP	PERSON TO CONTACT	TELEPHONE NUMBER
SCIENTIFIC INFORMATION RETRIEVAL	2515 OLD ORCHARD RD	SKOKIE	IL	60077	COHEN, ELI OR ANDERSON, GARY	312-470-9770
SOLITAIRE CORP	2355 N 25TH STREET	FRANKLIN PARK	IL	60131	SHETH, DINESH OR REENA	312-455-4711
STAVER COMPANY, INC.	41-51 SAXON AVENUE	BAY SHORE	NY	11706	LAZARUS, JEROME	516-666-8000
T.J. SPRADLIN, INC.	ROUTE 3 BOX 583	HOQUIAM	WA	98550	SPRADLIN, TIM	206-532-1485
TAYLOR-WILSON MFG. CO. INC	THOMPSON AVE	MCKEES ROCK	PA	15136	BRADLEY, WM OR KELLMAN, OTTO	412-331-3100
TECHNICAL CONSULTING TRADE CO	10325 RAY DRIVE	ROSCOE	IL	61102	NEWMAN, ROGER	815-623-6725
TOOLS & MACHINERY BUILDERS INC	HWY 72 E	ARCADIA	MO	63621	OWENS, STEPHEN, PRESIDENT	315-546-8938
TUREK & HELLER MACHINE, INC.	55 WEST LAURA DRIVE	ADDISON	IL	60101	TUREK, JOE OR HELLER, BUDDY	312-626-8777
WALPEX TRADING COMPANY INC.	1133 AVE OF THE AMERICAS	NEW YORK	NY	10036	PIRAINO, WALTER	212-921-8260
WARREN INDUSTRIES, INC	6003 FALCON ROAD	ROCKFORD	IL	61109	JACKSON, WARREN	815-874-9555
WASTE HEAT TECHNOLOGIES INC	189 NORTH MAIN STREET	WADSWORTH	OH	44281	FORMAZ, TIM S.	216-725-0571
WOOD FIBER MARKETING CORP	P O BOX 9545	SAVANNAH	GA	31412	STUBBS, WAYNE, EXEC VP	912-234-8131

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03/12/86

BORROWERS USING THE WORKING CAPITAL GUARANTEE PROGRAM SINCE INCEPTION OF THE PROGRAM

BORROWER	STREET	CITY	ST	ZIP	PERSON TO CONTACT	TELEPHONE NUMBER
WORLD TRADE IN COMPUTERS INC	2200 SAND HILL RD #240	MENLO PARK	CA	94025	SMITH, GORDON	415-DISCONT
XYLO CORP	RTE 3 P O BOX 4140	CORVALLIS	OR	97330	POSEY, P.L., PRESIDENT	405-469-4516

EXIMBANK

EXPORT-IMPORT BANK OF THE UNITED STATES
811 VERMONT AVENUE, NW
WASHINGTON, DC 20571

TELEPHONE (202) 566-2117

June 5, 1986

Mr. Stephen R. McSpadden
Counsel, Subcommittee on Commerce, Consumer
and Monetary Affairs
Committee on Government Operations
U. S. House of Representatives
Washington, D. C. 20515

Dear Steve:

In response to Chairman Barnard's letter of May 6, 1986, I am enclosing herewith Eximbank's comments on the points raised by witnesses at your hearings and in letters to the Subcommittee concerning our Working Capital Guarantee Program and the Bank's interest in supporting exports by export trading companies.

We would appreciate an opportunity to discuss this matter further with you at your convenience. I will call you shortly in this connection.

Sincerely,

Nancy

Nancy S. Pigman
Congressional Relations Officer

Enclosures

RECEIVED
JUN 6 1986
COMMERCE, CONSUMER AND
MONETARY AFFAIRS SUBCOMMITTEE

EXPORT-IMPORT BANK OF THE UNITED STATES

A. Discrepancies in previous data provided to the subcommittee

Eximbank considers a guarantee authorized when it is approved and charges its budget at that time even though the fee may not be paid and guarantee actually used for several months until the exporter obtains an order and draws on the guaranteed loan. For this reason, Eximbank provided the earlier list of authorized guarantees. A list is attached with the information concerning amounts approved, disbursed and fee paid.

Some comments are needed regarding the attached computer printout.

The Guarantee can cover either financing of specific transactions or a revolving line of credit financing various repetitive sales. An example of the former is Delta Brands which has been the recipient of four different guaranteed loans. When each product was shipped and payment received, the relevant guaranteed loan was paid off and Eximbank's guarantee expired.

An example of the latter is T.J. Spradlin. The amount of credit under the revolving line can rise and fall as advances are made and repaid with the balance varying daily. By the end of the guarantee period, total advances under the line may be several times the high credit approved which is shown under approval amount.

B. Complaints about and alleged problems with the Working Capital Guarantee Program.

As can be seen from the application form attached, Eximbank asks for the same kind of information the commercial bank asks for when the borrower approaches them for a loan. Additional information may be requested depending upon the nature of the transaction, e.g. if the loan is requested to produce goods to fulfill a specific contract, a copy of the contract will be requested.

The following comments relate to the specific issues raised:

"Unreasonable collateral": Generally inventory and accounts receivable are offered as collateral; however, Eximbank will consider requests with any reasonable collateral. The exporters generally buy or produce inventory, sell it generating a receivable and collect the receivable in the normal course of business-hence the usually offered inventory and accounts receivable. Eximbank's guidelines on collateral tend to be generous in that inventory purchased with the proceeds of a guaranteed loan is eligible collateral. For example, if the loan amount is $100,000, the Eximbank guaranteed loan will provide $90,000 and the exporter need only come up with $10,000 from its own resources. Usually commercial banks will only provide 40% to 50% funding on inventory ($40,000-$50,000 in above example) without our guarantee.

To our knowledge, no one has yet offered their personal home as principal security. Eximbank does require the guarantee of the principals on each Working Capital Guarantee, so by extension we would have their personal assets as additional collateral. However, it should be noted that this is principally required to keep the principals involved in the business. Most of these guaranteed loans are made to sole proprietorships or partnerships; if these principals leave the firm, the repayment prospects are reduced considerably. It should be noted that in one case where principal guarantees were not obtained, Eximbank paid a $623,000 claim.

Previously collateralized accounts receivable could be acceptable collateral if offered by the exporter and bank. However, usually accounts receivable generated by the sale of inventory bought or produced with the proceeds of a guaranteed loan are normally offered as collateral.

"Delays and lengthy application process"

Requests are usually presented to the Board of Directors between 2 and 4 weeks after all necessary information has been received. Frequently requests arrive at Eximbank with missing or outdated information which must be provided before the request can be acted on. Until the request is received at Eximbank, we cannot advise the bank what additional information is needed. In an effort to generate additional business, we frequently suggest the banker provide what information is readily available and we will contact him as soon as possible with what else is needed after we review the request.

"Continued requests for and large amounts of documentation"

We do not feel the information requested is unjustified. Our conversations with numerous bankers leads us to believe that we are asking for the same type of information they should be obtaining to make their own credit judgment. This is further substantiated by pp. 6 of Mr. Owens letter of May 7, 1986.

"Exim's administrative requirements or loan conditions (such as monitoring inventory, receiving invoices, etc.)"

We ask banks to exercise the same level of prudence on Eximbank guaranteed loans as they would on loans for their own risk. If collateral is required, some form of proving the collateral exists is needed. This may take the form of a UCC filing, periodic audits or samplings by the lender. Some banks have offered a lock-box approach where they will collect all receivables and pay suppliers. Eximbank provides a form which banks may use to substantiate the required collateral as an attachment to its guarantee agreement. Banks may use their own internally generated forms and approaches if they wish. It should be noted that the Eximbank format was copied from one provided by a commercial bank.

"Inability to guarantee standby letters of credit issued as advance payment, bid and/or performance guarantees"

One of the bright spots in the program has been the numerous transactions successfully completed involving the sale of capital equipment to the People's Republic of China. The Chinese will open letters of credit for the cash payment and progress payments but insist on the U.S. supplier providing its own letter of credit for the same amount so if the U.S. exporter does not ship the product, the buyer can reclaim all funds previously paid. The U.S. exporter does not get the benefit of the funds provided because they are needed to cash collateralize the performance letter of credit required by the Chinese. Eximbank's guarantee fits very well in this type of transaction by providing the funds necessary to produce the product.

Specific Comments:

Taylor-Wilson Manufacturing Co.

Mr. Kellman's comments involve excessive cost, documentation, collateral, etc. This guarantee was provided under Eximbank's joint program with the U.S. Small Business Administration. Except for the requirement that the loan be collateralized, the program guidelines and operation are entirely the judgment of the S.B.A. Eximbank is presented with the loan package by S.B.A. after their analysis and asked to participate equally with S.B.A. in the risk. Eximbank approved all requests as presented by S.B.A.

AEGIS

We are somewhat mystified by their statement that the program would work better for specific transactions than for guarantees of revolving credit lines since we believe the program is appropriate for either situation. This was the largest guarantee under this program. It was initially approved as a 90% guarantee of a $10 million line and amended to a 45% guarantee of a $20 million line. The latter made it easier for the commercial bank to administer as one line of credit. It may or may not have "foundered on Exim's request for personal guarantees". The principal owner, in meetings at Eximbank, stated he was willing to provide his guarantee. We were aware, however, of a large cash collateralized loan at another bank under which AEGIS would receive the large amount of collateral in the near future after our approval thereby obviating the need for the Eximbank guaranteed loan.

Tools and Machinery Builders

Unfortunately, Eximbank did not have a standardized guarantee in the early months of the program for lenders to review before applying under the program. We now provide lenders with copies of the guarantee so they can review it with counsel and senior management prior to using the program.

At the time of our approval, Eximbank was under the impression that a contract was imminent, hence the fee payment date was very short. We have been very accomodating on fee due dates under the program setting and/or extending these dates if the foreign transaction is not finalized.

Eximbank is of the opinion that a 1.5% fee for a 12 month guarantee is quite modest. We have seen under the program that many lenders will reduce their interest rates acknowledging Eximbank's guarantee. It should be noted however that Eximbank does not limit the fees lenders may charge and many lenders believe that the often risky credits involved justify a higher interest rate. Notwithstanding pp. 8 of Mr. Owens letter, the fee is charged on the loan amount, not on the value of the contract. For revolving lines of credit, the fee is based on the estimated high credit.

Mr. Howard Hammonds - IMPS

Many of Mr. Hammond's statements revolve around the financial condition of his now - bankrupt firm. Eximbank was very concerned about his firm's finances but approved the guarantee nonetheless. We were quite concerned over the firm's accounting practices (rather than write-off a bad debt from the firm's first Saudi dealer, it was given to IMPS for capital stock).

Obviously Eximbank does not compare applicants under the Working Capital Guarantee Program to Fortune 500 firms. If we did, neither IMPS or any other firm would be approved. We ask for information to find a reasonable assurance of repayment. Mr. Hammonds was of the opinion that this is an entitlement program and was reluctant to produce needed information hence the extended processing period. We do not, however, have the same information in his statement. For instance, we were under the impression that Equibank cancelled his credit due to payment difficulties.

Mr. Fred O. Oladeinde - Trans World Products

The views expressed by Mr. Oladeinde do not accurately characterize or reflect the attitude of either Eximbank or FCIA with respect to assisting export trading companies through our export credit insurance program. We have a strong interest in providing support to those companies who seek assistance; we do, of course, at the same time review eligibility in the context of exporter underwriting criteria. Mr. Oladeinde's views may have been influenced by FCIA's decision not to offer a short term insurance policy quote to Trans World Products. This decision was based solely on available information and commercial underwriting considerations and in no way should be construed or interpreted as reflecting a negative attitutde towards export trading companies. In addition, it is unclear that any inordinate delays were experienced on any specific applications which involved Trans World Products as a supplier. Our records in fact indicate that an application submitted by another party (on which Trans World was the supplier) was received by Exim in late August 1983 and approved by Eximbank in early September. This authorization was subsequently amended to accommodate a portion of the second transaction cited by Mr. Oladeinde (it was not utilitzed in part because requested documents were not submitted on a timely basis).

Finally, it should be noted that Trans World Products initial approaches to Eximbank involved support for sales to Nigeria which presented considerable risk due to the country's adverse economic conditions and outlook. Eximbank established a formalized program for this market in late 1983 which was designed to provide effective and timely support to U.S. exporters on a risk-acceptable basis. This program supported over $600 million of U.S. exports to Nigeria in the FY 1984-1985 period and has been accessible to all U.S. exporters, irrespective of the size or nature of a firm's operations, for qualifying transactions. We believe that Trans World Products could have readily availed itself of this support vehicle for its Nigerian business opportunities.

C. Eximbank does not separately allocate guarantee authority for the program. The program's guarantee authority is part of the overall insurance and guarantee authority for Eximbank.

OMB No. 3048-0003
Expires 5/31/87

EXPORT-IMPORT BANK OF THE UNITED STATES

APPLICATION FOR WORKING CAPITAL GUARANTEE

1. Name and Address of Applicant Lender:

2. Name and Address of Borrower/Exporter:

3. Type of Exporter (check one):
- a. Manufacturer of intermediate or consumable goods ____
- b. Manufacturer of capital equipment ____
- c. Producer of agricultural products ____
- d. Distributor/dealer/marketing agent ____
- e. Service company ____
- f. Other (specify) ____

4. Relationship of Borrower or Exporter to Lender:
- a. How long a customer ______________
- b. What exposure/experience ______________________________

____

5. Transaction Characteristics:
- a. Amount of loan ______________
  - (check one)
  - (1) transaction-specific ______________
  - (2) revolving ______________
- b. Term (months) ______________
- c. Security
  - (1) inventory (describe method of valuation) ______________________________

    ____
  - (2) receivables (Letters of Credit, Drafts, etc.) ______________________________

    ____
  - (3) guarantor (principals, others) ______________________________

    ____
  - (4) other (specify) ______________________________
- d. Product or service (SIC codes, if possible) ______________________________
- e. Export markets (be specific, if possible) ______________________________

  ____

  ____
- f. Cost to the exporter (percent per annum)
  - (1) interest rate ______________
  - (2) lender's fees (excluding pass-through of Eximbank guarantee and insurance fees) ______________

EIB Form 84-1
8/84

6. **Lender's *primary* reason for requesting Working Capital Guarantee:**
(for example: legal lending limits reached, credit risk, ability to reduce cost of financing due to reduced risk for lender, administrative/legal simplicity, U.S. Government backing required for foreign exposure, U.S. government backing required for small business, etc.):

7. **Indicate your borrower's primary purpose for this loan** (check one):
   a. To meet a one-time working capital need related to a large shipment to a new customer or initial exports. _____
   b. To provide working capital needed to maintain existing export activity or expand exports to more buyers. _____
   c. Other (specify) ____

8. **Is the resulting export transaction going to be covered by FCIA insurance, an Exim guarantee or private sector guarantee?** _____
(complete as applicable)
   a. FCIA (specify policy type) ____
   b. Other
      (1) Exim's Commercial Bank Guarantee Program _____
      (2) Medium Term Credit Program _____
      (3) Small Business Credit Program _____
      (4) Private insurance (specify) _____

9. **Please attach the following information:**
   a. A brief history of the Borrower and Guarantor, including the date organized, legal status and a description of its operations and major shareholders.
   b. Borrower's and Guarantor's signed or audited (if available) financial statements for the past three years including aging of receivables and breakdown of domestic and export sales.
   c. Projected financial statements for the period the loan will be outstanding showing an ability to service the additional debt to be guaranteed.
   d. Three recent credit reports and/or references.
   e. A short personal biography of principal owners and senior management.
   f. Signed personal financial statements of principal owners.
   g. Any additional information the applicant bank feels is relevant to this request.

The Applicant Lender certifies that the representations made and the facts stated by it in the application for a Working Capital Guarantee by the Export-Import Bank of the United States (Eximbank) are true, to the best of its knowledge and belief, and that it has not misrepresented or omitted any material facts relevent to said representations. The Applicant Lender agrees that such representations and facts shall form the basis on which an Eximbank guarantee may be given and that the truth of such representations and facts shall be a condition precedent to any liability of the guarantor thereunder. The Applicant Lender certifies that it does not have any actual knowledge and further certifies that it did not withhold any actual knowledge it had which could reasonably be expected to cause or tend to cause a loss to Eximbank under its guarantee. If after the date of this Application, the Applicant Lender comes into possession of any such knowledge, the Applicant Lender agrees not to withhold it and the undersigned agrees to immediately communicate such knowledge to Eximbank by telex or letter as appropriate.

The Applicant Lender understands that Eximbank's guarantee covers 90 percent of the loan amount and that any security that the Applicant Lender may arrange for its 10 percent risk retention, no matter in what form it may be, will be shared with Eximbank in the same proportion that Eximbank and the Applicant Lender share in the Risk of any loan made under Eximbank's guarantee. By signing and submitting this application, the Applicant Lender certifies that it would not be willing to make this loan without Eximbank's guarantee.

____
Name of Applicant Lender

By __________________________________
Signature

____
Title Telephone No.

EIB Form 84-1
8/84

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STATUS OF APPROVED WORKING CAPITAL GUARANTEES AS OF
MAY 21, 1986

UNITED STATES EXPORTER	AMOUNT OF LOAN APPROVED	APPROVAL DATE	AMOUNT DISBURSED TO DATE	EXPIRY DATE	TOTAL FEE PAID
DELTA BRANDS INC	833000	05/31/83	833000	09/30/83	8330
XYLO CORP	3300000	05/31/83	9768347	12/31/84	19080
SAXON EXPORT CORPORATION	400000	07/12/83	309950	07/31/84	3100
AEROTECH WORLD TRADE CORP	3000000	08/16/83	0	08/31/84	0
DELTA BRANDS INC	1350000	09/07/83	1350000	11/30/80	19224
WOOD FIBER MARKETING CORP	1000000	09/07/83	1000000	08/31/84	10000
TOOLS & MACHINERY BUILDERS INC	759000	09/13/83	0	09/30/84	0
KLUMB LUMBER COMPANY INC	2000000	10/24/83	1998000	10/31/84	35000
INTL MKT & PROCUREMENT SVCS INC	200000	12/13/83	0	12/31/84	0
MONARCH METALS CORPORATION	250000	12/20/83	0	12/31/84	3750
DELTA BRANDS INC	1700000	03/06/84	1700000	03/31/85	25500
WORLD TRADE IN COMPUTERS INC	800000	03/13/84	800000	04/30/85	12000
NORTH ATLANTIC TIMBER & SHIPPING	1500000	03/20/84	750000	09/30/85	7500
CUMBERLAND HARDWOODS INC	300000	04/03/84	300000	07/31/85	4500
DAVIS & BARRYMAN INTERNATIONAL	1500000	04/03/84	1500000	04/30/85	22500

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STATUS OF APPROVED WORKING CAPITAL GUARANTEES AS OF MAY 21, 1986

UNITED STATES EXPORTER	AMOUNT OF LOAN APPROVED	APPROVAL DATE	AMOUNT DISBURSED TO DATE	EXPIRY DATE	TOTAL FEE PAID
PLATTCO CORPORATION	800000	05/01/84	0	05/31/85	0
INTERNATIONAL CHIP & ASSOCIATES INC	2500000	05/22/84	0	05/31/85	0
AMERICAN EXPORT GROUP INTL SVCS INC	20000000	10/09/84	0	12/31/85	0
GENERAL ROBOTICS CORP	300000	10/18/84	300000	10/15/85	9000
J & M DISTRIBUTING CO., INC.	52500	12/07/84	52500	/ /	788
INTERCONTINENTAL CONSULTANTS INC	200000	12/20/84	161000	12/31/85	2700
R D SYSTEMS INC	700000	01/10/85	650000	08/31/85	7000
HETTINGA EQUIPMENT INC	403000	01/24/85	403000	09/30/85	453
JERNIGAN TRADING COMPANY INC	479000	01/24/85	497815	01/31/86	7500
BRETTRAGER MANUFACTURING CO.	1080000	02/07/85	1080000	02/28/86	16200
DCR INTERNATIONAL	25000	02/07/85	25000	12/19/85	0
FREMONT GROUP, LTD.	180000	02/07/85	170000	04/30/85	1800
PETRO-CHEMICAL SUPPLIERS, INC	500000	02/21/85	0	03/16/85	0
HETTINGA EQUIPMENT INC	433400	02/26/85	433400	12/26/85	488
TAYLOR-WILSON MFG. CO. INC	800000	03/01/85	0	09/30/85	0

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STATUS OF APPROVED WORKING CAPITAL GUARANTEES AS OF MAY 21, 1986

UNITED STATES EXPORTER	AMOUNT OF LOAN APPROVED	APPROVAL DATE	AMOUNT DISBURSED TO DATE	EXPIRY DATE	TOTAL FEE PAID
COMTEC ECONOMATION INC	200000	03/07/85	200000	09/30/85	3000
PHILIPPI HAGENBUCH, INC.	150000	03/19/85	140000	09/30/85	1500
HETTINGA EQUIPMENT INC	600000	03/28/85	0	06/30/85	0
J & M EXPORT, INC.	500000	04/02/85	500000	04/30/86	562
SCIENTIFIC INFORMATION RETRIEVAL	300000	04/05/85	300000	04/01/86	4500
RAMCO INC	253500	04/24/85	230500	05/31/85	2305
WASTE HEAT TECHNOLOGIES INC	305000	04/24/85	305000	10/31/85	3050
WALPEX TRADING COMPANY INC.	2000000	04/30/85	0	11/30/86	0
SOLITAIRE CORP	200000	05/10/85	290000	05/15/86	3000
MONARCH METALS CORPORATION	250000	06/06/85	0	06/30/86	0
ROSCOR CORP	3170000	06/13/85	3170000	07/31/86	47550
CUMBERLAND HARDWOODS INC	500000	06/20/85	500000	07/31/86	4500
GREAT WESTERN MEAT CO.	500000	06/21/85	501000	06/30/86	11250
COMTEC ECONOMATION INC	300000	06/27/85	300000	06/30/86	4500
TECHNICAL CONSULTING TRADE CO	300000	06/27/85	300000	07/31/86	5500
DYNEQUIP, INC.	150000	07/10/85	150000	07/15/86	2250
KLUMB LUMBER COMPANY INC	2000000	07/17/85	1600000	07/31/86	30000

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STATUS OF APPROVED WORKING CAPITAL GUARANTEES AS OF MAY 21, 1986

UNITED STATES EXPORTER	AMOUNT OF LOAN APPROVED	APPROVAL DATE	AMOUNT DISBURSED TO DATE	EXPIRY DATE	TOTAL FEE PAID
LOOPCO INDUSTRIES, INC.	600000	07/17/85	600000	03/31/86	6000
TUREK & HELLER MACHINE, INC.	750000	08/01/85	0	08/31/86	0
DELTA BRANDS INC	1800000	08/08/85	1731991	06/30/86	25080
LIVERNOIS ENGINEERING COMPANY INC	1000000	08/08/85	0	07/31/86	0
STAVER COMPANY, INC.	200000	08/27/85	200000	02/28/87	900
RESORCON, INC.	800000	08/28/85	0	02/28/87	0
RET CORPORATION	500000	08/29/85	450000	09/30/86	7500
WARREN INDUSTRIES, INC	190000	10/02/85	180000	05/01/86	1800
IBBERSON INTERNATIONAL INC	600000	11/07/85	0	12/31/86	0
NORTH ATLANTIC TIMBER & SHIPPING	750000	11/07/85	750000	09/30/86	11250
EDUCATIONAL INNOVATION SYSTEMS INC	1500000	12/19/85	1250000	12/31/86	22500
T.J. SPRADLIN, INC.	750000	12/19/85	748000	12/31/86	11250
IBBERSON INTERNATIONAL INC	550000	01/21/86	550000	06/30/86	2750
JERNIGAN TRADING COMPANY INC	500000	01/23/86	478815	01/31/87	7264
EXPORT MGMT INTL INC	50000	02/07/86	500000	12/31/86	375

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STATUS OF APPROVED WORKING CAPITAL GUARANTEES AS OF
MAY 21, 1986

UNITED STATES EXPORTER	AMOUNT OF LOAN APPROVED	APPROVAL DATE	AMOUNT DISBURSED TO DATE	EXPIRY DATE	TOTAL FEE PAID
*** Total ***	69563400		40007318		

D. EXIMBANK'S RESPONSES TO QUESTIONS SUBMITTED BY SUBCOMMITTEE MEMBER, REPRESENTATIVE ALBERT G. BUSTAMANTE

UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

NATIONAL SECURITY AND
INTERNATIONAL AFFAIRS DIVISION

APR 2 3 1986

Mr. Stephen R. McSpadden
Commerce, Consumer, and Monetary
Affairs Subcommittee
Room B-377
Rayburn House Office Building
Washington, D.C. 20515

Dear Steve:

Enclosed is a copy of the Eximbank's responses to questions submitted by Congressman Bustamante. As arranged with Mr. Gene Fisher, Legislative Assistant to Congressman Bustamante, we have forwarded the answers directly to him.

Please call if you have any questions.

Sincerely yours,

John E. Watson

Allan I. Mendelowitz
Associate Director

Enclosure

RECEIVED
APR 2 8 1986
COMMERCE, CONSUMER AND
MONETARY AFFAIRS SUBCOMMITTEE

EXIMBANK

EXPORT-IMPORT BANK OF THE UNITED STATES
811 VERMONT AVENUE NW
WASHINGTON DC 20571
TELEPHONE (202) 566-2117

April 18, 1986

Mr. Louis Lucas
Assistant Regional Manager
United States General Accounting Office
Suite 1907, 100 Summer Street
Boston, Massachusetts 02110

Dear Mr. Lucas:

As requested in your letter of March 26, 1986, enclosed are the answers to Congressman Albert G. Bustamentes questions regarding Eximbank programs under the Export Trading Company Act of 1982.

If there are any further questions, please contact me.

Sincerely yours,

James K. Hess
Treasurer-Controller

April 17, 1986

Question: Which loan guarantee programs are targeted to small businesses, and are they sufficient incentive to reduce the financial risk exposure on new-to-export and new-to market firms?

Answer: Eximbank offers a number of programs targeted to small businesses to assist them in financing their U.S. exports. These programs are especially helpful to those companies who are new to exporting.

First, the Working Capital Guarantee Program helps exporters get the financing they need for their pre-exporting activities. This program guarantees the private lender (who would not have extended the working capital line without Eximbank's guarantee) that, if the exporter defaults, Eximbank will repay 90 percent of the outstanding loan. Thus, the small business is able to access the working capital necessary to fulfill its obligations to foreign buyers.

Eximbank's Exporter Credit Insurance Program provides exporters protection against the risk that the foreign purchaser will not pay. Two insurance policies under the program are specifcally designed to cater to the needs of small businesses. The New-To-Export policy is offered with greater coverage than on policies available to more experienced exporters. Additionally, small businesses may be insured under an Umbrella Policy administered by banks, export trading companies and other financial and professional organizations. This policy lessens the paperwork burden on the small exporter and can help him obtain financing, as policy proceeds are assignable to any financial institution as collateral.

Small businesses can also benefit from the Commercial Bank Guarantee Program, which encourages commercial banks to make loans to foreign purchasers of U.S. goods by reducing their risk. Thus, a bank may be more willing to finance export sales by small businesses if such sales are guaranteed by Eximbank.

Finally, Eximbank's Small Business Credit Program enables U.S. banks to offer medium-term, fixed rate export loans to finance sales by small U.S. companies. As interest rates are fixed at the lowest rates permitteed under the guidelines followed by OECD members, small businesses are generally assured of being in the position to offer repayment terms to foreign purchases that match those of officially supported foreign competition. The small U.S. company is therefore able to compete on an equal basis with foreign firms to win export contracts.

Thus, Eximbank offers a variety of program's particularly suitable for small businesses. Access to these program's is possible by contacting Eximbank, any Foreign Credit Insurance Association's regional offices or the various Department of Commerce branch offices around the country.

Question: Is there more concern about preparing loan packages for large rather than small exporters, and does Eximbank devote more resources to large-volume loan packages than small?

Answer: Eximbank processes applications for its various programs on a case-by-case basis. Emphasis is not placed on the size of the exporter or the sale but is rather placed on such factors as the political and economic condition of the country the goods will be sold to, the creditworthiness of the foreign buyer and the credit terms being offered. These factors determine the amount of concern and resources devoted to any particular transaction.

Because some small businesses are more inexperienced than others in both exporting and Eximbank programs, applications for assistance from such entities involve a greater amount of processing time. For example, some of the most in depth preparations and processing is done for the working capital guarantee program, which is targeted soley for small businesses who cannot get working capital without Eximbank assistance.

Additionally, a good deal of time is devoted to educating potential exporters, a majority of them small, through seminars, conferences and telephone conversations. Eximbank's Marketing Division, along with members of various divisions within the bank, visit exporters and banks all over the United States in an attempt to familiarize them with Eximbank programs.

Question: If so, how does this affect small businesses who usually have small export transactions?

Answer: See answer to Question #2.

Question: How successful ha the program been in attracting small, new-to-export and new-to-market fir to exporting?

Answer: In order to attract he small, and new-to-export company, Eximbank's Marketing Division has been rrying on a two stage educational program:

1. Educating the American co ercial banking community, through an intensive four day seminar, about the hanics of Eximbank programs including, of course, the Working Capital arantee Program.

2. A direct one-on-one calli program on small and medium sized companies who have never or only occasiona y exported to explain how, through their commercial bank, and using Eximbank pro ams, export sales can be safely and profitably undertaken.

This careful, time consuming ut very important effort has begun to pay real dividends as we see more and re smaller, or new-to-export companies availing themselves of the Working Ca al Guarantee Program through their commercial banks.

Question: Identify the small and medium-sized businesses that have received loan guarantee under the program, and indicate those that are new-to-export or new-to-market firms.

Answer: (See attached)

Question: What is the range of interest rates charged to firms by the banks and are they low enough to induce small businesses to look to exporting as a means of expanding sales?

Answer: (See attached)

Question: Complete the following table.

Lender	Borrower	Amount	Interest Rate	Indicate whether firm is new-to-market or new-to-export

Answer: (See attached)

EXPORT-IMPORT BANK OF THE UNITED STATES

WORKING CAPITAL GUARANTEES ISSUED FROM THE INCEPTION OF THE PROGRAM THROUGH APRIL 10, 1986

(Pursuant to P.L. 97-290; October 8, 1982)

The following provides the name of the lender, loan recipient, and the loan amount in dollars. A code is shown indicating if the borrower is small, medium-size, new-to-export or new-to-market. The listing is provided in alphabetical order according to the name of the lender. Eximbank uses the definition of small business as defined by the SBA. A medium-size business is not formally defined but it is generally interpreted to be a business larger than small but not a major corporation. Eximbank's qualifying definition for a new-to-export business specifies that the average annual export sales during the preceding two years must not exceed $750,000. If the preceding fiscal year was the firm's first year of export sales, sales may not exceed $1,000,000. If the company meets one of these two criteria, it is then eligible for new-to-export services for five years. Eximbank does not have a formal definition of new-to-market but for purposes of this report, new-to-market will be defined as a firm having exported to a given market for less than five years.
Key to Codes:

1: Small business
2: Medium-size business
3: New-to-market
4: New-to-export

The interest rate charged to the borrower is not in the Eximbank database; however, a review of the cases shows the rates to vary between prime and prime + 4%, with the majority clustered around prime + 2%. Eximbank guarantees interest to the participating bank at a rate of Treasury + 1% for U.S. government borrowings of corresponding maturities.

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04/15/86

LENDER	BORROWER	LOAN AMOUNT	1=SMALL 2=MEDIUM-SIZE 3=NEW-TO-MARKET 4=NEW-TO-EXPORT
ALBANY BANK & TRUST CO. CHICAGO IL	SCIENTIFIC INFORMATION RETRIEVAL SKOKIE IL	300000	1
ALLIED MEMORIAL BANK HOUSTON TX	INTERNATIONAL CHIP & ASSOCIATES INC HOUSTON TX	2500000	2,3,4
AM. NAT. BK. & TRU. CO. OF CHI CHICAGO IL	ROSCOR CORP MOUNT PROSPECT IL	3170000	2
AMERICAN BANK HOUSTON TX	PETRO-CHEMICAL SUPPLIERS, INC HOUSTON TX	500000	1,3,4
AMERICAN SECURITY BANK, N.A. DISTRICT OF COL DC	RET CORPORATION SPRINGFIELD VA	500000	1,3
ARIZONA BANK PHOENIX AZ	COMTEC ECONOMATION INC FLAGSTAFF AZ	200000	1
ARIZONA BANK PHOENIX AZ	COMTEC ECONOMATION INC FLAGSTAFF AZ	300000	1

LENDER	BORROWER	LOAN AMOUNT	1=SMALL 2=MEDIUM-SIZE 3=NEW-TO-MARKET 4=NEW-TO-EXPORT
BANCO PORTUGUES DO ATLANTICO NEW YORK NY	DELTA BRANDS INC IRVING TX	1350000	1
BANCO PORTUGUES DO ATLANTICO NEW YORK NY	DELTA BRANDS INC IRVING TX	1800000	1
BANK OF GRAYS HARBOR ABERDEEN WA	T.J. SPRADLIN, INC. HOQUIAM WA	750000	1
BANK OF LA COSTA CARLSBAD CA	RAMCO INC SAN DIEGO CA	253500	1,3,4
BANKERS TRUST CO DES MOINES DES MOINES IA	HETTINGA EQUIPMENT INC DES MOINES IA	403000	1
BANKERS TRUST CO OF DES MOINES DES MOINES IA	HETTINGA EQUIPMENT INC DES MOINES IA	433400	1
BANKERS TRUST OF DES MOINES DES MOINES IA	HETTINGA EQUIPMENT INC DES MOINES IA	600000	1
BAY BANK OF MIDDLESEX BURLINGTON MA	NORTH ATLANTIC TIMBER & SHIPPING HARDWICK MA	750000	1

LENDER	BORROWER	LOAN AMOUNT	1=SMALL 2=MEDIUM-SIZE 3=NEW-TO-MARKET 4=NEW-TO-EXPORT
CENTERRE BANK,NA ST LOUIS MO	TOOLS & MACHINERY BUILDERS INC ARCADIA MO	759000	2,3
CENTRAL FIDELITY BANK VIENNA VA	INTERCONTINENTAL CONSULTANTS INC ARLINGTON VA	500000	2,3
CENTRAL NAT. BANK OF CLEVELAND CLEVELAND OH	WASTE HEAT TECHNOLOGIES INC WADSWORTH OH	305000	2,3,4
CHEMICAL BANK WHITE PLAINS NY	PLATTCO CORPORATION PLATTSBURGH NY	800000	2,
CHEMICAL BANK NEW YORK NY	WALPEX TRADING COMPANY INC. NEW YORK NY	2000000	2
COMMERCE UNION BANK NASHVILLE TN	SAXON EXPORT CORPORATION MIAMI FL	400000	1
COMMERCIAL CREDIT BUS LOANS INC CHAMBLEE GA	KLUMB LUMBER COMPANY INC CRYSTAL SPRINGS MS	2000000	1

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LENDER	BORROWER	LOAN AMOUNT	1=SMALL 2=MEDIUM-SIZE 3=NEW-TO-MARKET 4=NEW-TO-EXPORT
COMMERCIAL CREDIT BUS LOANS INC CHAMBLEE GA	KLUMB LUMBER COMPANY INC CRYSTAL SPRINGS MS	2000000	1
CONNECTICUT NATL BANK HARTFORD CN	AEROTECH WORLD TRADE CORP WHITE PLAINS NY	3000000	1
EQUIBANK PITTSBURGH PA	INTL MKT & PROCUREMENT SVCS INC BUTLER PA	200000	2
FIR. AM. BK. & NAT. BK. WASH. DISTRICT OF COL DC	AMERICAN EXPORT GROUP INTL SVCS INC WASHINGTON DC	20000000	2
FIRST INTERSTATE BK OF WASH SEATTLE WA	J & M EXPORT, INC. SEATTLE WA	500000	1,3,4
FIRST NATIONAL BANK & TRUST CO ROCKFORD IL	SOLITAIRE CORP FRANKLIN PARK IL	200000	1,3,4
FIRST NATIONAL BANK & TRUST CO ROCKFORD IL	TECHNICAL CONSULTING TRADE CO ROSCOE IL	100000	1,3,4

LENDER	BORROWER	LOAN AMOUNT	1=SMALL 2=MEDIUM-SIZE 3=NEW-TO-MARKET 4=NEW-TO-EXPORT
FIRST NATIONAL BANK & TRUST CO ROCKFORD IL	WARREN INDUSTRIES, INC ROCKFORD IL	190000	1
FIRST STATE BANK MORTON TX	GREAT WESTERN MEAT CO. MORTON TX	500000	1
FIRST WISC NATL BANK OF MIL MILWAUKEE WI	GENERAL ROBOTICS CORP HARTFORD WI	300000	2
FIRST WISCONSIN NATIONAL BANK MILWAUKEE WI	EDUCATIONAL INNOVATION SYSTEMS INC FONTANA WI	1500000	1
HARRIS TRUST & SAVINGS BANK CHICAGO IL	TUREK & HELLER MACHINE, INC. ADDISON IL	750000	1
LIBERTY STATE BANK & TRUST TROY MI	DCR INTERNATIONAL SOUTHFIELD MI	25000	2,
LIBERTY STATE BANK AND TRUST TROY MI	J & M DISTRIBUTING CO., INC. UTICA MI	52500	2

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LENDER	BORROWER	LOAN AMOUNT	1=SMALL 2=MEDIUM-SIZE 3=NEW-TO-MARKET 4=NEW-TO-EXPORT
MARINE BANK, N.A. MILWAUKEE WI	R D SYSTEMS INC ROSCOE IL	700000	2,3
MARINE BANK, N.A. MILWAUKEE WI	PHILIPPI HAGENBUCH, INC. PEORIA IL	150000	2,3
MARINE BANK, N.A. MILWAUKEE WI	RD SYSTEMS, INC. ROSCOE IL	300000	2,3
MARINE MIDLAND BANK NEW YORK NY	DELTA BRANDS INC IRVING TX	833000	1
MARINE MIDLAND BANK NEW YORK NY	DELTA BRANDS INC IRVING TX	1700000	1
MARYLAND NATIONAL BANK BALTIMORE MD	JERNIGAN TRADING COMPANY INC KNOXVILLE TN	479000	1
MARYLAND NATIONAL BANK BALTIMORE MD	JERNIGAN TRADING COMPANY INC KNOXVILLE TN	500000	1
MELLON BANK NA PITTSBURGH PA	TAYLOR-WILSON MFG. CO. INC MCKEES ROCK PA	800000	1

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LENDER	BORROWER	LOAN AMOUNT	1=SMALL 2=MEDIUM-SIZE 3=NEW-TO-MARKET 4=NEW-TO-EXPORT
MICHIGAN NAT. BK. OF DETROIT DETROIT MI	LIVERNOIS ENGINEERING COMPANY INC DEARBORN MI	1000000	2,3
N.Y. BUSINESS DEVELOPMENT CORP ALBANY NY	STAVER COMPANY, INC. BAY SHORE NY	200000	1,3,4
NATIONAL BANK OF DETROIT DETROIT MI	BRETTRAGER MANUFACTURING CO. SAGINAW MI	1080000	1
NATIONAL STATE BANK ELIZABETH NJ	MONARCH METALS CORPORATION NEW YORK NY	250000	1,3,4
NATIONAL STATE BANK ELIZABETH NJ	MONARCH METALS CORPORATION NEW YORK NY	250000	1,3,4
NORTHERN TRUST COMPANY CHICAGO IL	FREMONT GROUP, LTD. CHICAGO IL	180000	2,3
NORWEST BANK MINNEAPOLIS, N.A. MINNEAPOLIS MN	DYNEQUIP, INC. ST. PAUL MN	150000	2
NORWEST BANK MINNEAPOLIS, NA MINNEAPOLIS MN	IBBERSON INTERNATIONAL INC MINNEAPOLIS MN	550000	2,3

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LENDER	BORROWER	LOAN AMOUNT	1=SMALL 2=MEDIUM-SIZE 3=NEW-TO-MARKET 4=NEW-TO-EXPORT
NORWEST BANK OF MINNEAPOLIS NAMINNEAPOLIS MN	IBBERSON INTERNATIONAL INC MINNEAPOLIS MN	600000	2,3
PALMER NATIONAL BANK DISTRICT OF COL DC	WORLD TRADE IN COMPUTERS INC MENLO PARK CA	400000	1
PARK BANK OF FLORIDA ST. PETERSBURG FL	EXPORT MGMT INTL INC TAMPA FL	50000	2
SAVANNAH BANK & TRUST CO. SAVANNAH GA	WOOD FIBER MARKETING CORP SAVANNAH GA	1000000	1
SEATTLE FIRST INTL BANK SEATTLE WA	XYLO CORP CORVALLIS OR	3300000	2,3,4
SOCIETY NATIONAL BANK CLEVELAND OH	LOOPCO INDUSTRIES, INC. TWINSBURG OH	600000	1
SOUTHTRUST BANK BIRMINGHAM AL	DAVIS & BARRYMAN INTERNATIONAL RUSSELLVILLE AL	1500000	1

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LENDER	BORROWER	LOAN AMOUNT	1=SMALL 2=MEDIUM-SIZE 3=NEW-TO-MARKET 4=NEW-TO-EXPORT
STATE STREET BANK & TRUST CO BOSTON MA	NORTH ATLANTIC TIMBER & SHIPPING HARDWICK MA	1500000	1
THIRD NATIONAL BANK NASHVILLE TN	CUMBERLAND HARDWOODS INC SPARTA TN	300000	1
THIRD NATIONAL BANK NASHVILLE TN	CUMBERLAND HARDWOODS INC SPARTA TN	500000	1
UNION NATL BK OF PITTSBURG PITTSBURGH PA	RESORCON, INC. PITTSBURGH PA	800000	1,3

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APPENDIX 7.—POSITION PAPER BY THE INDUSTRY SECTOR ADVISORY COMMITTEE ON SMALL AND MINORITY BUSINESS FOR TRADE MATTERS

INDUSTRY CONSULTATIONS PROGRAM

EXPORT FINANCE

A Position Paper by the Industry Sector
Advisory Committee on Small and
Minority Business for Trade
Policy Matters

ISAC 14

U.S. Department of Commerce

United States Trade Representative

1984

INTRODUCTION

The Industry Consultations Program, jointly sponsored by the U.S. Department of Commerce and the Office of the U.S. Trade Representative, is a mechanism which provides the U.S. Government with advice from representative elements of the business community which are affected by U.S. trade policy decisions. The Program is Congressionally mandated by the Trade Act of 1974 and the Trade Agreements Act of 1979.

One of the 17 sectors represented in the program is the Industry Sector Advisory Committee on Small and Minority Business for Trade Policy Matters (ISAC 14). It has identified export finance as the major concern of its sector and has devoted time and effort in examining ways to enhance exports through better export financing programs.

This Export Finance paper represents the views of the Committee on government programs and policies on export finance and recommends the necessary action the Government needs to take to increase the competitiveness of its small and minority business sector. The paper is a companion piece to the Sector Profile of ISAC 14 in the Industry Consultations Program Sector Profiles, published by the Trade Advisory Center, U.S. Department of Commerce.

EXP RT FINANCE

A Positi Paper by the
Industry Sector dvisory Committee on
Small and nority Business
for Trad Policy Matters

Introduction

This position paper is a follow up to the Sector Profile originally prepared by the Industry Sect Advisory Committee on Small and Minority Business for Trade Po cy Matters (ISAC 14) sponsored by the Secretary of Commerce and he U. S. Trade Representative. It addresses the vital area of ex rt finance as it affects small and minority businesses (SMBs). T purpose of this paper will be to attempt to take some of the ystery out of a subject that is complex, subtle, and incomplete understood by the general public.

We will not deal with the urgency of the international trade situation except to observe tha

1. The trade deficit is soa ing out of control.

2. SMBs may be the last ditch trade deficit remedy. The evidence is now ove whelming that big business and government are approac ng the end of their traditional remedies, and labor most likely to proceed toward destructive protectionis

This paper is an offer of a ne perception of SMBs which will be iconoclastic in terms of "what verybody knows," but may be closer to some basic understandings fro which new action guidelines may be drawn.

General Limitations

ISAC 14 is a private sector ad sory group with a relatively small handful of consistently active members who meet periodically at their own time and expense to eview international trade affairs. Internally, there is industrio serious commitment, and a high level of common agreement on issues. There are some important limits to the potential impact o ISAC 14, however.

With literally hundreds, perhaps thousands, of government personnel active in the policy on operatic al areas of international trade, it is impossible for ISAC 14 to mor tor everything simultaneously. At meetings, important time is dec cated to presentations by relevant government personnel regarding u ates and new issues as they emerge, to which ISAC members feed back what they hope will be valuable insights from the firing line. Over the course of ISAC 14 history, some important patterns of thought in government perception of SMBs have taken shape, and it will be the purpose of this paper to reinforce some and challenge many others. It will not be possible to offer a comprehensive critique of all of the past, present, and potential future export finance issues. Rather, by limited examples chosen from these issues we would hope to make some new thought available.

What Makes ISAC 14 Businesses Different?

An important element in the Sector Profile of ISAC 14, cited above, was its offer of the organic morphology of SMBs, rather than statistical description. This matter is so critical to "finding the handle" on small business that it is important to make some of these points again for the purpose of small business as this paper would deal with it.

We will not deal with businesses which are "small" or "minority" by sales, asset size, employment, percentage of racial constitution by ownership or work force, or any of the other traditional statistical approaches. Instead, it is imperative that we look at small businesses as primary cells of capitalism, especially in considering their financing. It is imperative because the subject at hand, exporting, is an important business risk/opportunity to which capitalistic response is being solicited and measured. What special characteristics do SMBs have in their primitive capitalism that will make them different creatures with which to deal than the big businesses which have been America's primary exporters of the past?

Nothing is more important to export finance than the capital structure and the basic business question of a capitalist society: "Who takes the risk, and who gets the return?" Instantaneously, the difference between small and big business is strikingly evident.

The capital bases of small businesses tend to be individual, family, or a very limited group of private investors. They have drawn their equity capital from personal, family, or intimately known financial resources. Their business borrowings are invariably made against owner/manager personal guarantees. Investors also tend to be direct participating members of management.

Big business, by contrast, tends to be run on a publicly held capital base unencumbered by the personally guaranteed debt of its owners. Policy passes through a board of directors which may likely have more or less indirect management participation, or even ownership, in the company. Operational day-to-day management is conducted by hired professionals.

Obviously, there are shades of gray in these interpretations of small and big business, but it is the mass tendencies which have to be dealt with, and these lead to two profoundly different characteristics:

1. Large businesses are managed to yield after-tax per-share earnings directed at producing dividend streams and/or capital gains attractive to public investors.
2. Small businesses are managed primarily to control risk within acceptable levels, then within these levels provide salaries, bonuses, perks, and future personal security to the investors/managers who own/operate them.

The financing of big and small business, including possible successful Federal export financing, must accommodate these differences. The key factor for the SMB looking at any new opportunity, including exporting, is: "Who takes the downside risk, and what are the failure consequences?" This is the acid test, and it is the most consistently misunderstood characteristic of small business by all of the "Bigs" (government, business, and labor). It is the pervasive source of failure of decades of policy in the SMB international trade area.

Why Are Businesses Small?

A close corollary to this misperception of small business is the structure of misperception as to why any business is small. It has become popular in big business to minimize the importance of small business in export trade for obvious self-serving purposes in competition for the limited resources of government. Two classic examples in circulation at the moment are the "Grace Report" and the Boeing position paper, "The Invisible Exporters," which imply that the SMB component of export business opportunity can be derived from subcontract subservience to large exporters such as Boeing, a sort of "feeding the horses to nourish the birds." Realistically, small business has a vital independent stature in exporting which will not be possible to exploit until some of these popular myths have been dispensed with.

Some small businesses are small only as a matter of timing over which nobody has any control. Every big business started as a small one, and some of the most important, exciting big businesses of America's future will come from products and enterprises which are now at the very beginning of their growth curve. It becomes important, then, that we have programs in position that can offer instant assistance to all small business in exporting, and stop trying to identify future winners with fad expressions like "high tech" for export support programs. Technical and investment analysts are simultaneously trying to identify these future growth companies with skill, experience, and sophistication far beyond that available to any crystal ball owned by any agency of government. The marketplace will very rapidly identify the big winners, at home and abroad; and without export support for SMBs in general, the markets abroad will be sacrificed perhaps before they can ever be reached, among the little companies which might be destined to be big.

Other companies are small simply because they are highly specialized, and the total market demand for their offerings simply won't command the existence of a big company as a supplier. They will never be big within the scope of their existing business, but they may be old, stable, well-managed, and offering top quality products at world competitive prices. With appropriate export support, perhaps thousands of these companies could build an international marketplace for American industry which would stabilize our export strength for decades to come, as opposed to trying to pick out the next IBM, or gambling on nature and politics for a bumper crop of agricultural exports.

Most important, this kind of SMB diversity would be essentially invulnerable to the contemporary common complaint of foreign supplier "targeting" in U.S. and world markets.

Other small businesses may be small by the nature of their products or services which will not bear the cost of transportation. Conceivably these might open foreign branches and grow into big businesses and important overseas earners by small business replication. (The annual sales volume or market area of a McDonald's hamburger stand is a small business by any definition, whether in Philadelphia or Dusseldorf.)

Small businesses are not small because their owners are necessarily unenterprising. It is worth noting that this presumed cause of small business reserve in exporting is almost invariably offered by those who are not operating a small business of their own in these times.

Most important in the area of exporting, however, is the unrelenting, all-pervasive, staggering misconception that management of small businesses is too obtuse. Small business owners supposedly need "information." If they would accept government "education" they would become happy and profitable exporters. Thus, after literally decades of how-to-do-it books, pleadings by all of the agencies of government, seminars, and every conceivable form of communication that can be sent their way, small business operators are still unmoved to enter exporting in the way which reflects their potential, and the nation's need. The easy rationale is "They are too dumb," but would it be possible to test the opposite conclusion, "They might be too smart"? It is possible that small business operators, with their dedication and sensitivity to risk limitations, have sensed in all of the government's messages to export a far more important subliminal message which persuades them they should not.

The Misguidance of Government Policy and Programs

No matter what the superficial content of the "education" on exporting afforded small business in the past, there have been two clear, unmistakable Federal government messages for small business:

1. With trivial exception, government policy and programs are calculated to isolate government from participating in the business risk of small firms in exporting.

2. The trend of very recent years has been to dramatically escalate the diversion of export business risk away from government to small business, in spite of the escalation of the trade deficit.

There have been fringe cosmetic actions such as export trading company legislation and proposed relaxation of the foreign corrupt practices law, but at the capitalist ground level of business risk-taking the government has relentlessly opened up the maximum possible distance between itself and small business. This has not been lost on the small business community, either consciously or unconsciously, as SMBs consider exporting as a business risk. Although condemned for a lack of astuteness or sensitivity to the government's message that SMBs should be exporting for their own benefit if not for the government's, the average astute small business operator cannot miss the fact that the government is fleeing full tilt from its own good idea. In the face of this example, what SMB operator can persuade himself to risk a lifetime's investment, savings, income source, and future retirement base?

The examples of government isolation from small business export investment risk appear in a broad variety of forms beyond the scope of this paper, but some examples would be the following:

1. In spite of statistics on numbers of transactions involving small business (which are heavily loaded by inclusion of the Foreign Credit Insurance Association (FCIA) program), the Export-Import Bank does virtually all of its foreign buyer financing to the benefit of big business.

2. The Small Business Administration (SBA) a few years ago heavily publicized the availability of one hundred million dollars in financing for the export activities of small companies. What was not publicized was that this did not increase funding, but merely allowed loan officers to open existing SBA programs to exporting purposes. Characteristically, these loans include security agreements structured to financially crush any business and personally destroy its owners unable to repay as scheduled. (The new revolving export credit line at SBA also has comparable security arrangements.)

3. Commerce has relentlessly withdrawn its financing participation in foreign trade fairs which are programmed principally to the benefit of new and/or small exporters. In those in which they now participate, it is arguably cheaper for participants to buy the services from independent sources than to pay Commerce "user fees."

4. Within the last two to three years, Commerce has introduced astronomical (in some cases multi-hundred percent) increases in fees for export mailing lists, agent-distributor service searches, credit reports, new product publicity, and the other small business support offerings across the spectrum.

5. The Domestic International Sales Corporation (DISC) has been the windfall tax blessing to big exporters, but since it assumes no downside risk (promising only to take away less of what might be earned by a small business that takes the primary risk), only the most unreconciled apologists for DISC can continue to argue its merits. The forthcoming Foreign Sales Corporation (FSC) appears to be more of the same, made slightly more complicated. ISAC 14 is studying the legislation and will recommend amendments for inclusion in the bill.

6. Congress has congratulated itself on the new export trading company legislation, using the choice of a name to equate it to "America's answer to the Japanese model." Actually, it merely eliminates a few uniquely American antitrust and banking legal technicalities, but emergence of the export risk benefits to small business have been far more proposed in theory than realized in practice. The silence in the banking and export community grows more ominous, as the awaited wave of new exporting companies to be formed under this legislation has not yet appeared in functional form. Will it ever?

While it is laudatory to proclaim that the government does not belong in the business risk arena, and that more Yankee Trader spirit is needed by SMBs, it is common knowledge that the government protects the business risk of dairy and tobacco farmers, jet plane manufacturers selling abroad, businesses operating in flood zones, and a whole myriad of manifestations of the personal and business lives of all Americans. This tends only to exaggerate the government's past and increasing present reluctance to support SMBs at the risk level in exporting.

What, then, needs to be done?

The Basis of Federal Responsibility

Actually, one of the most important immediate needs may be one of the most subtle, as well as (fortuitously) earliest to be answered. It is the need for the government to pull itself together. The international trade reorganization proposal, whatever else its merits or drawbacks, may afford the government the chance to speak with a single voice to the export needs of the SMB community, as well as invite some approachable entity toward which SMBs may reach.

The traditional complaint of SMBs is that big government is impenetrable. In international trade, it is virtually unidentifiable. So many agencies and branches of the government proclaim their dedication to the service of small business exporting that bewilderment is universal. Everyone is "coordinating" everyone else, and the buck stops nowhere.

Incidentally, the character of this problem for small business is not limited to the Federal government. At the regional, state, county, municipal, and port authority levels, there are government, quasi-government, and independent agencies of various capability and responsibility all desperately claiming to coordinate the efforts of each other in the essentially nonexistent programs to create a small business exporting front.

It is the feeling of ISAC 14, however, that by its nature international trade is the responsibility of the Federal government as derived from the Constitution. Government is directly responsible for the preservation of the value of the national currency, and there are too many practical as well as legal limitations for lower levels of government to cross American borders and conduct commercial or legal diplomacy. The buck cannot be passed down.

What Are the Financial Needs?

At the export finance level, the SMB exporter needs two basic forms of low-risk support: pre-export and receivables. For the moment, we will leave "low-risk" undefined and address it in more detail later.

In the pre-export scene, there is a need to identify markets, both by geography and product/service demand, adapt products to the markets, participate in demand stimulation activities, establish channels of distribution, build exportable inventories, and provide for and/or train export management. This is the high risk phase of the process where some form of venture capital seed money is needed, rather than hard loan financing.

Beyond the point of actually developing orders for goods to be shipped in export, there is a need for financing which will permit small American exporters to competitively finance these orders at minimal risk to themselves and turn over their own capital as safely and quickly as possible.

It would be impossible to develop within the context of this paper a comprehensive program or series of programs that would answer to all of these needs, but a few examples might be in order: Front-end venture capital, or operational aid for foreign advertising, foreign business development travel, overseas trade fair participation, agent and distributor research, credit information on prospective foreign buyers, product modification to foreign standards, preparation for foreign language advertising and other communications, and training programs for management in exporting. There should also be inventory finance for the buildup of exportable inventory--raw materials, work in process, and finished goods--with security limited to the goods themselves and not the general assets or the personal resources of the small business.

For foreign sales receivables, there is a need for competitive financing to foreign buyers of SMBs comparable to that offered by the Export-Import Bank to big business customers. As a corollary, but not replacement, export credit insurance should be available, without onerous recourse provisions and deductibles, to provide true minimal-risk export financing for small American exporters to their customers.

As cited above, it would be impossible to completely outline the details of what the above program should be, but as an example of what is possible, the attached exhibit describes one British program aimed at the small business market there. Note that government risk exposure is subject to repayment on royalties, rather than secured debt, and that the entire thrust of the program is to create exporters rather than minimize government exposure.

It is vital to emphasize that programs are feasible -- and would undoubtedly be welcomed by SMB new exporters -- that provide government direct participation in the pay-back of success. Actually, the indirect benefits of successful integration of SMB exporting would be far more important in the reduction of unemployment and the trade deficit. However, to those who would turn a blind eye to these benefits and regard any Federal funding of SMB exports as charity, this need not necessarily be the case.

The Administrative question of who gets what among SMBs soliciting government participation in their own export plans is beyond the scope of this paper, but would not appear insurmountable. Research and innovation programs are already being administered to support this kind of endeavor in SMBs, and while they may not be perfect, they do appear functional. And while the British model in the attached exhibit may not be ideal for our purposes, it suggests an important realization.

A psychological threshold has been crossed in the British government, as well as several others in the world, which has not yet been reached in America:

> It is in the interest of the national government to join as true risk partners with the small and minority business entities of the private sector to protect the national business position in international trade. The scope of venture financing is perhaps most important at pre-export levels, but must cover participation through the buyer-payment phase.

The Nature of Government SMB Export Finance Programs

Although the needs are summarized above without detail of programs, in addition to minimal risk any program would require some other important features:

1. They must be available to small business at minimal risk and at reasonable cost, if they are not to be outright grants to the indirect ultimate benefit of the nation. An absolutely vital part of the cost that will make or break any program will be, in modern slang, the "hassle" required to afford small businesses a chance to participate. Blizzards of forms falling from blankets of bureaucrats will spell certain death to anything other than the most certain chance of getting gratuitous charity. Inventory loans must bear reasonable interest rates, or receivables financing must be available at competitive rates--competitive in international trade, not only U. S. money markets.

2. As a corollary of (1) there must be painstaking organization of delivery systems of programs to small business. There is the immediate risk of escalation of bureaucracy because small businesses tend to run in large numbers, they lack massive staffs to conduct government relations, and their business affairs tend to require government speed and decisiveness--often with less comprehensive business decision-making information than might be available from a business giant. A new brand of bureaucrat with a new sensitivity to small business may have to be created in the personnel offices of a new Washington agency to handle this type of thing. In summary, no matter how imaginative the policy or well-conceived and comprehensive the program, a flawed delivery system will negate any other effort.

3. As new programs of the recommended type come into being, there will need to be new techniques for monitoring results, post-auditing the efforts of government and small business involved, and regenerating directive action as well as positive reinforcement. We can no longer afford "more of the same" in the disaster area of financing SMB export efforts. It is time for those of any political persuasion to ask: "If not us, who, and if not now, when?"

Conclusion

SMBs are emerging as the last resort in combating the trade deficit, which is skyrocketing. It would be valuable to determine within classical economics which would be more devastating to the American economy if we reach the end of 1984 and have to choose between a one-hundred-billion-dollar foreign trade deficit and a two-hundred-billion-dollar Federal budget deficit. *New and different* Federal export financial effort in one form or another is going to be at the heart of any initiative to integrate small and minority businesses into the American exporting community, and this will only work with minimal-risk type financing. The only source of this kind of financing is going to be the Federal government, which in the past has been aloof and is now withdrawing. Export-Import Bank/FCIA Programs, weak and without delivery systems, and SBA prohibitively secured lending, constitute tokenism at best.

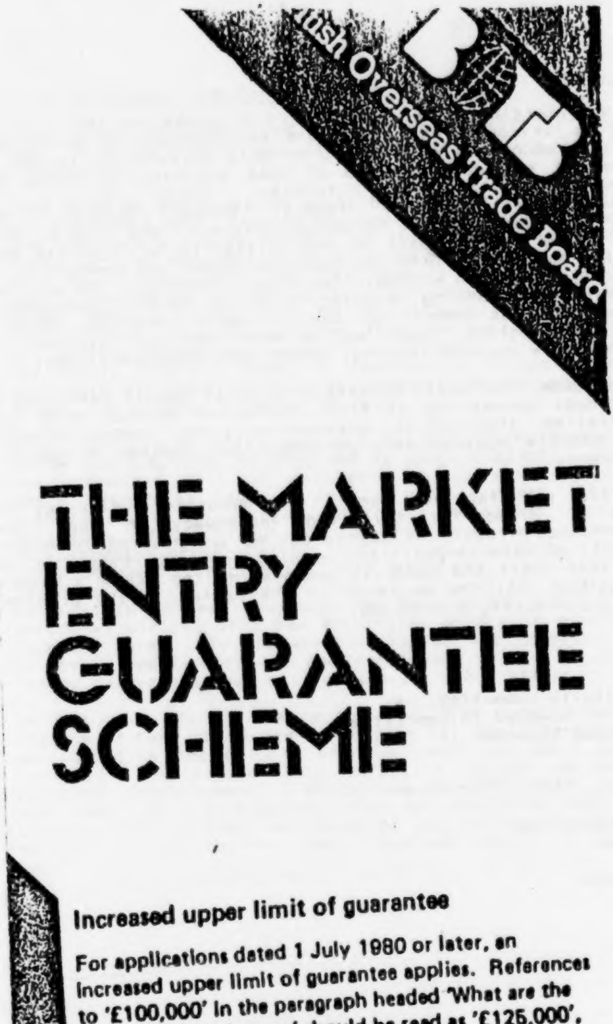
Although American small private enterprise people have long been the traditional mainspring of free enterprise coupled with government conservatism, they cannot, unaided and alone, compete effectively in world markets against foreign competitors backed by *their* foreign governments.

Voiceless and faceless, small and minority businesses bear the stigma of blame for perceived inadequacy in the theater of international trade. If day to day we are haunted by deterioration of our trade balance position, nothing seems to change including the theme that small and minority business is the nation's weakness. Is it possible that the weakness of the nation is the problem of its small and minority businesses?

Respectfully submitted, as
prepared, amended in Committee,
and passed November 17, 1983

Erwin von Allmen
Chairman

Attachment



itish Overseas Trade Board

THE MARKET ENTRY GUARANTEE SCHEME

Increased upper limit of guarantee

For applications dated 1 July 1980 or later, an increased upper limit of guarantee applies. References to '£100,000' in the paragraph headed 'What are the limits to the assistance' should be read as '£125,000', and the figure '£200,000' as '£250,000'.

THE MARKET ENTRY GUARANTEE SCHEME

The Market Entry Guarantee Scheme (MEGS) is designed to help smaller and medium sized firms in manufacturing industry to deal with the financial risk and problems associated with a venture to develop a new export market. In approved cases, the Scheme will contribute 50% of the eligible costs of the market venture in return for a levy on sales receipts which is intended to recover the contributions with a commercial rate of return on the Scheme's investment. If, by the end of the agreed venture period, sales have not materialised as expected, then no further levy payments are required and the firm and the Scheme will share the loss. For this guarantee, the firm pays the Scheme an annual premium.

The scheme is being operated on a trial basis for two years with limited funds. Assistance under the scheme is discretionary and will be offered so as to provide a spread of ventures by size, product and market. Applicants will be expected to put forward a package of proposals which constitute a well-planned marketing programme for the development of an additional export market and to demonstrate their capability to carry this out. Applicants must clearly show that their objective is to obtain a substantial increase in the volume of their exports over the period of the venture and thereafter, to the benefit of the United Kingdom.

Who can apply ?

The scheme is open to firms in manufacturing industry. Firms must be exporting a tangible product manufactured in the United Kingdom and the Standard Industrial Classification (prepared by the Central Statistical Office and published by HMSO) will be used as a guide. Orders III to XIX in the SIC will normally be accepted as 'manufacturing'.

Firms mounting a marketing attack on a new overseas market on behalf of either a single manufacturer or group of manufacturers can be considered. Applications from such companies, including export merchants, etc, will have to show that they are acting as the manufacturer's sales organisation and are under firm contract to the manufacturing firm over an acceptable period. In such cases, the manufacturer(s) may also be required to be contractually liable to the scheme for the levy on sales, and satisfactory arrangements to ensure that eligible costs are incurred solely in support of the products on whose sales the levy is charged will have to be agreed.

What projects and costs are eligible ?

The scheme is aimed at helping firms with the implementation phase of a new export market entry venture and not with the market research or exploration phase. (Other sources of assistance are available for this phase and potential applicants who have not completed this phase should seek guidance from BOTB offices as detailed at the end of this note.) Proposals for assistance must describe a well-planned sales attack based on a substantial examination of the market. Single elements such as a publicity campaign on its own or a visiting programme in isolation will not be eligible. Similarly, the venture must involve the continuity of sales in the new market and not individual sales/projects. The market should be defined in terms of sales area using national or local boundaries and by product; and the eligible costs must relate exclusively to this product and market combination. A new market is one in which the firm has not been selling or in which it has some sales but plans a major increment involving substantial new costs.

To be eligible for support, costs must broadly be overhead costs which are written off as incurred (eg not capital investment) and are largely irrecoverable (except in the sense of recovery from margin on sales). They must *not be directly* related to the manufacture and distribution of the product (eg manufacturing costs, transport costs and agents' commission are not eligible). To be eligible, costs must be incurred solely and directly in relation to the venture and its defined product and market combination. Costs already incurred by a firm in respect of activities prior to the date of application are not eligible, nor can continuing costs for existing facilities be considered.

Costs will normally be considered for eligibility in the following categories:

1. Overseas office accommodation

Rental; property and contents insurance; maintenance; cost of services; local property taxes, office equipment and consumable supplies; purchase and running costs, or rental, of cars. Where premises are purchased not rented, the lesser of interest charges on the capital cost or an imputed rent will be considered for eligibility.

2. Staff costs

For firm's overseas-based administration, sales or warehouse staff: salaries; employment taxes; expenses (excluding entertainment); recruitment and relocation costs. Costs of the firm's technical support staff are only eligible if they are not part *of the after-sales service and maintenance requirements and their services are not charged to the customer.*

3. Training

Training in the selling and servicing of the product(s) of overseas-based staff including non-company staff (eg agents).

4. Travel and expenses

Travel and subsistence expenses for the firm's overseas-based staff; and for home-based staff when visiting the defined market in connection with the venture. Entertainment costs are not eligible.

5. Sales promotion

Advertising; publicity; sales literature (specific to the defined market); product demonstration.

6. Costs of holding stock

The term stock covers both the product and its spare parts. Costs of showrooms and storage facilities under similar headings to those for office accommodation. Transport costs for the product or spare parts are not eligible. Financing of stock, including interest charges, is not eligible nor is stock loss due to deterioration, obsolescence or other causes.

7. Commercial and legal costs

Legal costs of setting up the overseas operation and external audit costs; costs/fees for patents, licences, trademarks, testing and approval of product to necessary local standards.

A firm's cost of participating in an export marketing activity which has been supported by other sources of public funds will not be eligible. The nature of eligible costs are such that, in most cases, assets are not created. However, the scheme will have a right to a proportion of the proceeds of sale of any assets to whose costs it has contributed (eg office equipment and cars) if the scheme does not recover all contributions with interest.

How does the scheme work ?

A proposal put forward by a firm will be studied by the MEGS Unit and, if an offer of assistance is made and accepted, then an agreement will be signed. This agreement will include a definition of the product(s) and market area, the planned eligible costs in each year under agreed headings, the length of the investment period, the subsequent recovery period and the rate of levy on sales receipts. For each year of the investment period, the firm pays the scheme 3% of the scheme's 50% contribution to the planned eligible costs for that year as a premium in respect of the guarantee (ie that the contributions do not have to be repaid if the venture does not succeed). For each year of the investment period, the scheme pays the firm 50% of those eligible costs actually incurred under each heading. The total contribution in each year cannot be more than 50% of the total planned eligible costs. For each year of both the investment period and the recovery period, or until the scheme has recovered its contributions with a commercial rate of interest, the firm pays the scheme the agreed rate of levy on all actual sales receipts for the defined market/product(s) combination. The length of the investment and subsequent recovery periods and the rate of levy will be set so that there is a good expectation that the scheme will recover its contributions with a commercial rate of return before the end of the recovery period. If the end of the recovery period is reached before the scheme has made full recovery on this basis, then no further levy payments are required.

What are the limits to the assistance ?

The scheme's contributions to eligible costs for one venture cannot be more than £100,000 and must be a minimum of £20,000. The investment period cannot be longer than five years and the recovery period will normally be at least as long as the investment period. There are no limits on the size of firm or size of project but the scheme is intended for smaller and medium sized firms and the £100,000 limit on contributions and the fact that the levy is charged on all sales receipts in the defined market makes the scheme less suitable for new market entry programmes with eligible costs over £200,000.

Financial arrangements

The premium for the first year must be paid within one month of the date of agreement and then within three months of the start of each year of the investment period. Contributions to eligible costs will be payable by the scheme in respect of each year of the investment period and will normally be made when the necessary financial statement for the year has been received and evaluated. Interim payments can be considered. The levy due on sales receipts is payable within three months of the end of each year of the investment and recovery periods until it ceases. During the investment period, the levy due will normally be netted off the contributions to eligible costs.

The firm will be required to provide certificated returns of costs incurred and sales receipts for the venture, signed by a responsible officer of the company and validated by an independant accountant. The contributions to eligible costs by the scheme do not create a debt or liability in the normal sense and no security or collateral is required (the firm will be required to give evidence of its financial viability in the proposal). The levy is an agreed rate of levy on sales receipts (normally as invoiced) and is not considered as a direct repayment of the contributions to eligible costs. In respect of each year's trading (or when interim payments are made), the previous balance will be brought forward, the interest calculated for the period and the latest payment of contributions added in, the latest levy payment deducted, and the new outstanding balance carried forward. The interest rate to be used will be 2½% above a weighted average of the clearing banks' base rate rounded to the nearest ¼% for the period in question.

A firm will be entitled to withdraw from the scheme at the end or middle of any year, having given three months' notice, on condition that it pays at the withdrawal date a levy equal to all contributions to date, less any previous levy payments, with interest. There are no restrictions on firms withdrawing from the venture or any particular element of it but there will be a requirement to give notice of any significant changes of plans. The levy on sales will continue on the agreed basis even though the venture may effectively have been abandoned. If a firm incurs in any year of the investment period less than 25% of the planned eligible costs for that year, then the Government may at its discretion terminate the agreement at the end of that year, making no further contributions and recovering no further levy. Both contributions to costs and levy on sales receipts will be planned and dealt with in sterling terms and the agreement will specify the procedure for conversion from foreign currencies. In general for tax purposes, the scheme's contributions will be treated as reducing the firm's expenditure in respect of which

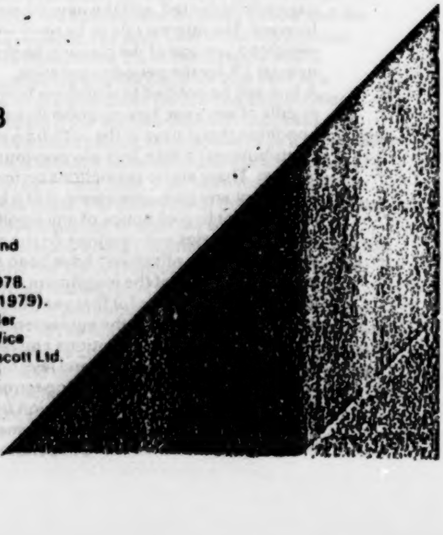
they are paid and the premium for the guarantee and levy payments will be treated as allowable deductions.

Applications

Application forms can be obtained from Export Services and Promotions Division at Export House, 50 Ludgate Hill, London EC4M 7HU or the Export Sections of the Department of Industry's Regional Offices, the Welsh Office Industry Department in Cardiff, the Scottish Office in Glasgow, the Northern Ireland Department of Commerce in Belfast and from British Overseas Trade Board (MEGS Unit), Department of Trade, Room 206, 1 Victoria Street, London SW1H 0ET. London.

***Note:* This document is a general guide to the scheme and shall not be regarded as constituting an offer of assistance or of forming part of any contract which may be entered into.**

January 1978



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Office of Private Sector Liaison
Office of the United States Trade Representative
Private Sector Advisory Committees
MEMBERSHIP REPORT BY COMMITTEE
ISAC14

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Office of the United States Trade Representative
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MEMBERSHIP REPORT BY COMMITTEE
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Macon, GA 31206

APPENDIX 8.—SUBCOMMITTEE CHAIRMAN BARNARD'S LETTER OF APRIL 23, 1986, TO HOUSE BANKING COMMITTEE CHAIRMAN ST GERMAIN CONCERNING FRB REGULATIONS

DOUG BARNARD, JR., GEORGIA, CHAIRMAN
JOHN M. SPRATT, JR., SOUTH CAROLINA
JOE KOLTER, PENNSYLVANIA
BEN ERDREICH, ALABAMA
ALBERT G. BUSTAMANTE, TEXAS

NINETY-NINTH CONGRESS
Congress of the United States
House of Representatives
COMMERCE, CONSUMER, AND MONETARY AFFAIRS
SUBCOMMITTEE
OF THE
COMMITTEE ON GOVERNMENT OPERATIONS
RAYBURN HOUSE OFFICE BUILDING, ROOM B-377
WASHINGTON, DC 20515

LARRY E. CRAIG, IDAHO
PATRICK L. SWINDALL, GEORGIA
H. JAMES SAXTON, NEW JERSEY

MAJORITY—(202) 225-4407

April 23, 1986

Hon. Fernand J. St Germain, Chairman
Subcommittee on Financial Institutions Supervision,
Regulation and Insurance
Committee on Banking, Finance and Urban Affairs
Room B-303 - RHOB
Washington, D.C. 20515

Dear Chairman St Germain:

I am writing to bring to your attention serious problems with the Federal Reserve Board's regulations governing export trading companies and, given the Board's refusal to modify them, to urge your consideration of possible legislation, within your subcommittee's purview, to overturn those regulations.

The House Subcommittee on Commerce, Consumer, and Monetary Affairs, which I chair, held a hearing on March 4, 1986, to examine the impact and implementation of the Export Trading Company Act, focusing particularly on Title II, the Bank Export Services Act. The General Accounting Office, Senator Heinz, Congressman Bonker, and senior officials of Chase Trade and First Chicago Bank testified that the Federal Reserve Board's regulations on export trading companies (ETCs) are unrealistic, unnecessary and burdensome. In particular, they focused their criticism on (a) the FRB's rule limiting ETC inventory to $2 million, (b) FRB's requirement that an ETC's export revenue amount to at least 50 percent of total income (and that all income from countertrade necessary for the export, count against the 50 percent threshold), (c) the FRB's prohibition on the export of services by an ETC, (d) the FRB's 10:1 asset to capital leveraging ratio for an ETC, and (e) the application of Section 23a of the Federal Reserve Act (the collateral and affiliate lending restrictions) to bank ETCs. Criticisms "a" - "d" could be addressed administratively by the Fed, whereas criticism "e" apparently requires a legislative solution.

Clearly, the weight of the testimony established that the Fed rules negatively impact the viability of bank ETCs, appear unreasonable and even unnecessary, and contravene congressional intent. Despite FRB assertions of flexibility — that it is ready and willing to waive the regulations in special cases — such waivers are not a substitute for sound regulation. Moreover, it took Chase Trade 11 months to obtain a limited waiver from the Fed on the leveraging requirements, notwithstanding the need to move quickly in international transactions. Normally, I would suggest a concerted effort to prevail upon the Fed to modify its regulations. However, the Fed is unwilling to modify its regulations and remains steadfast — if not obstinate — on the correctness of its position. (You may recall that the Board opposed this legislation.) It appears, therefore, that a legislative correction will be required for all the problems enumerated at the hearing.

Senator Heinz, whose testimony I have enclosed (together with the GAO report and other witness statements), has introduced S. 1934 to address these problems and override some of the FRB regulations. Also, as I understand, Congressman Bonker is presently drafting a bill, most of which will contain the same provisions as the Heinz bill (although with some improvements). Since any amendments to the Bank Export Services Act are clearly within your subcommittee's jurisdiction, I wanted to encourage you to look into this matter and suggest that we might jointly introduce remedial legislation for your subcommittee's consideration. I would be happy to work with you on it. Stephen McSpadden, a staff counsel to my subcommittee, is ready to provide your staff with any information or assistance.

With warm personal regard, I am,

Sincerely,

Doug Barnard, Jr.

Doug Barnard, Jr.
Chairman

Enclosures

cc: Richard Still

DB:srm:b

APPENDIX 9.—JUSTICE DEPARTMENT VIEWS ON THE PROBLEMS WITH AND THE NEED FOR CHANGES TO THE ANTITRUST PROVISIONS OF THE EXPORT TRADING COMPANY ACT

DOUG BARNARD, JR., GEORGIA, CHAIRMAN
JOHN M. SPRATT, JR., SOUTH CAROLINA
JOE KOLTER, PENNSYLVANIA
BEN ERDREICH, ALABAMA
ALBERT G. BUSTAMANTE, TEXAS

NINETY-NINTH CONGRESS
Congress of the United States
House of Representatives
COMMERCE, CONSUMER, AND MONETARY AFFAIRS
SUBCOMMITTEE
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COMMITTEE ON GOVERNMENT OPERATIONS
RAYBURN HOUSE OFFICE BUILDING, ROOM B-377
WASHINGTON, DC 20515

LARRY E. CRAIG, IDAHO
PATRICK L. SWINDALL, GEORGIA
H. JAMES SAXTON, NEW JERSEY

MAJORITY—(202) 225-4407

April 28, 1986

Hon. Edwin Meese III
Attorney General
  of the United States
Department of Justice
Washington, D.C. 20530

Dear Mr. Attorney General:

On March 4, 1986, the House Subcommittee on Commerce, Consumer, and Monetary Affairs held a hearing on the implementation and impact of the Export Trading Company Act of 1982. I request that the Justice Department provide its views on the implementation of the antitrust provisions of the Act, Title III, and the need for any legislative clarifications.

During the March 4th hearing, the representative from the U.S. Commerce Department, Mr. James Lacy, director of the Office of Export Trading Company Affairs, testified that there is still considerable debate among members of the antitrust bar on the level of antitrust protection provided under the Act and that "steps to create even greater certainty in the Title III provisions of the Act may help clarify" the situation. On March 21, 1986, the subcommittee sought elaboration on this point and on other matters, asking the Commerce Department to describe this ambiguity and uncertainty among members of the antitrust bar and also asking for suggested changes to clarify the situation. (My March 21st letter to Mr. Lacy is attached.)

It is my understanding that the Commerce Department is unable to recommend legislative changes because of a decision by OMB that our request requires a joint interagency response involving the Antitrust Division of the Justice Department, which administers the Title III provisions concurrently with the Commerce Department. Accordingly, I request that the Antitrust Division give this matter its prompt attention and furnish its views to OMB by June 1. Having the Administration's views on any problems with the Title III provisions and any suggestions or recommendations for legislative changes are essential to a subcommittee report on this important issue.

I would like Antitrust Division staff to keep subcommittee staff counsel Stephen McSpadden abreast of this Justice Department's progress in this matter. Please contact Mr. McSpadden if there are any questions.

Sincerely,

Doug Barnard, Jr.

Doug Barnard, Jr.
Chairman

Enclosure

DB:SM:b

cc: Mr. John Filippini
Antitrust Division

Mr. James C. Miller, III
Director
Office of Management and Budget

U.S. Department of Justice

Office of Legislative and Intergovernmental Affairs

Office of the Assistant Attorney General

Washington, D.C. 20530

07 JUL 1986

Honorable Doug Barnard, Jr.
Chairman, Subcommittee on Commerce,
Consumer, and Monetary Affairs
Committee on Government Operations
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

This letter responds to your April 28, 1986, letter to the Attorney General, in which you asked that the Justice Department provide its views on the implementation of the antitrust provisions of the Export Trading Company Act of 1982. You also asked our views as to whether there is a need for any legislative clarifications to Title III of that Act.

As you know, the Antitrust Division of the Department of Justice administers Title III concurrently with the Department of Commerce. The Department of Justice has worked closely with the Department of Commerce in promulgating regulations under the Act and in implementing its provisions. We have developed detailed guidelines that explain how our agencies will apply the statutory language and that provide several practical case studies. These guidelines have received favorable comment from persons interested in the Export Trading Company Act program. By explaining the agencies' analysis and providing illustrative examples, the guidelines clarify the law and encourage applications. In the formal processes that we and the Department of Commerce have established and in the close informal working relationship we have developed, both agencies strive -- in large measure successfully, we believe -- to apply the statute in a clear, understandable, and consistent manner that is in accord with congressional intent.

From your letter you appear to perceive some ambiguity in the Administration's view as to the current need for legislative changes in Title III. In order to correct any misunderstanding that may exist, the Department of Justice fully endorses Mr. Lacey's statements in testimony before your Subcommittee on March 4 and April 22 of this year to the effect that the Administration has no legislation to propose at this time but plans to continue to monitor Title III to determine whether any statutory changes may be desirable in the future.

We believe the export trade certificate program has operated successfully within the present statutory framework. While further experience with the program may lead us and the Department of Commerce to the conclusion that statutory amendments may be desirable, that is not the Administration's present view.

We very much appreciate this opportunity to clarify the Administration's position.

The Office of Management and Budget has advised this Department that there is no objection to the submission of these views from the standpoint of the Administration's program.

Sincerely,

R. Bolton

John R. Bolton
Assistant Attorney General